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ABSTRACT

Hearings on student loan consolidation are presented. Only the Student Loan Marketing Association (Sallie Mae) has the authority to consolidate student loans and that authority--scheduled to expire on August 1, 1983-- is being reviewed. State guarantee agencies have requested the statutory authority to consolidate loans. The findings of a study by the General Accounting Office (GAO) and the position of the Department of Education are included in the testimony. GAO studied consolidation, the current and projected costs of consolidation, the imapct of loan consolidation on defaults, and the capability of the states to consolidate loans, along with potential legislative modifications affecting program expansion, interest rates, minimum loan amounts, and interest subsidies. Sallie Mae offers three repayment options to borrowers participating in the loan consolidation program--a constant, monthly repayment schedule; and two types of graduated repayment schedules. Since the program has been operating only 1 year, it is too early to assess the impact on loan defaults. Testimonies of the representatives of state guarantee agencies, Sallie Mae, and banking institutions are provided. A Sallie Mae student loan application form is included, along with instructions and supplementary information. (SW)

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STUDENT LOAN CONSOLIDATION

JOINT HEARINGS

BEFORE THE

SUBCOMMITTEE ON POSTSECONDARY EDUCATION

OF THE

COMMITTEE ON EDUCATION AND LABOR

HOUSE OF REPRESENTATIVES

AND THE

SUBCOMMITTEE ON

EDUCATION, ARTS AND HUMANITIES

OF THE

COMMITTEE ON

LABOR AND HUMAN RESOURCES

UNITED STATES SENATE

NINETY-EIGHTH CONGRESS

FIRST SESSION

HEARINGS HELD IN WASHINGTON, D.C.
MAY 25, AND JUNE 8, 1983

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STUDENT LOAN CONSOLIDATION

WEDNESDAY, MAY 25, 1983

HOUSE OF REPRESENTATIVES, SUBCOMMITTEE ON POSTSECONDARY EDUCATION, COMMITTEE ON EDUCATION AND LABOR, JOINT WITH SENATE SUBCOMMITTEE ON EDUCATION, ARTS AND HUMANITIES OF THE SENATE COMMITTEE ON LABOR AND HUMAN RESOURCES,

Washington, D.C.

The subcommittees met, pursuant to call, at 2 p.m., in room 2175, Rayburn House Office Building, Hon. Robert Stafford (chairman of the Senate Subcommittee on Education, Arts and Humanities) presiding.

Members present: Senator Stafford, Representatives Simon, Harrison, Jeffords, and Petri.

Mr. SIMON [presiding]. The Subcommittee of the House on Postsecondary Education and Senate Subcommittee on Education, holding a joint hearing on student loan consolidation.

I will enter my statement in the record. We have some time problems here.

[Opening statements of Chairman Simon and Chairman Stafford follow:]

OPENING STATEMENT OF HON. PAUL SIMON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF ILLINOIS, AND CHAIRMAN, SUBCOMMITTEE ON POSTSECONDARY EDUCATION

Today the Subcommittee on Postsecondary Education and the Senate Subcommittee on Education hold a joint Arts and Humanities hearing on student loan consolidation. By law only the Student Loan Marketing Association (Sallie Mae) has the authority to consolidate student loans and that authority is scheduled to expire on August 1, 1983. State guarantee agencies have requested the statutory authority to consolidate loans.

The Education Amendments of 1980 (Public Law 96-374) granted loan consolidation authority exclusively to Sallie Mae. Over the last two years the Association has used that authority to consolidate over $100 million in Guaranteed Student Loans (GSL's) and National Direct Student Loans (NDSL's). During consideration of the Student Financial Assistance Technical Amendments of 1982, state guarantee agencies requested the authority to consolidate student loans. At that time, the Congress was unsure of the implications of such an extension on Federal costs and had not as yet reviewed the activities of Sallie Mae in their consolidation program. The conferees decided that before any further legislation was enacted regarding consolidation, the General Accounting Office should review the loan consolidation program and report on its findings to Congress.

The report language accompanying Public Law 97-301 specifically directed GAO to investigate the following issues in regard to consolidation: The need for legislative change in the current authority under which Sallie Mae consolidates loans, specifically addressing whether or not Sallie Mae has the capability when consolidating loans, to average varying interest rates of three percent and five percent; the capability of state loan guarantee agencies to consolidate student loans and the capability of state agencies to average varying interest rates of such loans which may in-

clude NDSL loans carrying interest rates of three to five percent; the potential savings to the Federal Government by expanding consolidation authority to state guarantee agencies; and the need for a minimum aggregate loan size under consolidation provisions and what limits would be appropriate.

The Subcommittees also requested that GAO provide general cost estimates on how much loan consolidation costs the Federal Government as it is presently carried out by Sallie Mae and how much it would cost if state guarantee agencies were also allowed to consolidate loans. GAO has now completed the requested study and are here today to report on their findings. At the same time that the Congress requested the study, it also provided that Sallie Mae's authority to consolidate loans would lapse on August 1, 1983 without further legislative action. However, the Congress made it clear that they did not intend for the authority to expire but that they did feel it was necessary to review the existing law and potentially rewrite the statute.

Based on the information we receive here today our Subcommittees will be meeting to discuss what direction we want to take in providing for future consolidation authority. Along with GAO we will also be hearing from Dr. Edward Elmendorf, the Assistant Secretary for Postsecondary Education, on the Department of Education's position on loan consolidation.

At this time I would like to welcome Senator Stafford and the Subcommittee on Education, Arts and Humanities and ask Senator Stafford for any opening remarks he would like to make.

OPENING STATEMENT OF HON. ROBERT T. STAFFORD, A U.S. SENATOR FROM THE STATE OF VERMONT AND CHAIRMAN, SENATE SUBCOMMITTEE ON EDUCATION, ARTS AND HUMANITIES

I am pleased to join with my good friend and colleague, Paul Simon, to conduct this joint hearing on the findings of the General Accounting Office with respect to the consolidation of student loans.

In order to provide some background to this study, I would like to review the history of loan consolidation. In the Education Amendments of 1980, Congress authorized the Student Loan Marketing Association (Sallie Mae) to consolidate the loans of students with multiple loans exceeding $5,000, or with a single loan exceeding $7,500, in order to afford students with high indebtedness the opportunity to reduce their monthly payments by extending the repayment period. Congress in 1980 clearly intended loan consolidation as a mechanism for preventing defaults.

In considering last year's higher education technical amendments, the Senate heard testimony from certain State loan guarantee agencies indicating that they could consolidate loans on the same basis as Sallie Mae, at lower cost to Federal Government, and that they should be afforded an opportunity to compete in the consolidation market with Sallie Mae. The provisions of the Senate version of the technical amendment, S. 2852, included such authority by the States. In conference, however, it became clear that there would be no final agreement between the House and Senate as to consolidation, since it was difficult to gauge the costs of consolidation under Sallie Mae, and would equally be difficult to assess the prospective costs of consolidation under a State agency-managed program.

Therefore, in an effort to achieve compromise, the conferees agreed to suspend Sallie Mae's consolidation authority as of August 1, 1983 and to direct GAO to conduct a study of consolidation, its current and projected costs, and the capability of the States to consolidate loans on the same basis as Sallie Mae. I do not believe that the conferees intended to allow loan consolidation to lapse absolutely—we clearly intended that the GAO report provide us with accurate information so that an adequate program of consolidation could be authorized by Congress in advance of the August 1 deadline.

We are pleased to have Mr. Morton Henig of GAO with us today to discuss the findings of the study. My good friend Dr. Edward Elmendorf of the Department of Education will be our second witness. We look forward to your testimony and your help in our efforts to come up with a strong program of consolidation.

Mr. SIMON. Senator Stafford will be here shortly. I am going to turn the chair over to my colleague from Vermont—this may be an all Vermont day here very shortly—temporarily until Senator Stafford gets here, and then we will hear from the witnesses.

My apologies to the witnesses. You have been around here long enough to understand.

Mr. JEFFORDS. Fine.

Mr. Henig, why don't you proceed?

STATEMENT OF MORTON HENIG, SENIOR ASSOCIATE DIRECTOR, HUMAN RESOURCES DIVISION, GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY ALBERT B. JOJOKIAN, GROUP DIRECTOR, HUMAN RESOURCES DIVISION; WILLIAM A. SCHMIDT, PROJECT MANAGER, HUMAN RESOURCES DIVISION; DONNA BEILVIN; AND JOAN DENOME

Mr. HENIG. Thank you, Mr. Jeffords.

I would like to introduce other members of the General Accounting Office who are here with me today. My name is Morton Henig. I am a senior associate director for the General Accounting Office. On my left is Mr. Al Jojokian, group director with the Human Resources Division, GAO. On my right is Bill Schmidt. He is the program manager, project manager for this particular assignment. I also have behind me Donna Beilvin and Joan Denome, who worked on the assignment.

I have a statement for the record which has been submitted. I will try and summarize that a little bit, take a little less time.

We are pleased to be here today to discuss the information you requested us to develop concerning the Student Loan Marketing Association's [Sallie Mae's] loan consolidation program. Specifically, we were requested to develop information on program costs and the program's impact on defaults, and on potential legislative modifications affecting program expansion, interest rates, minimum loan amounts, and interest subsidies.

The loan consolidation program is intended to reduce a borrower's repayment burden by providing extended repayment periods and lower monthly payments on relatively high student loan indebtedness. Repayment terms jointly developed by Sallie Mae and the Department of Education can vary from 10 years for loans of up to $7,500 to 20 years for loans totaling more than $16,000.

Sallie Mae began consolidating student loans in November 1981, and by December 31, 1982, had consolidated 10,648 loans totaling $66.9 million from 5,473 borrowers. About 70 percent of the consolidated loans exceeded $10,000. By April 1983, the consolidated loans had reached $107 million.

Sallie Mae offers three repayment options to borrowers participating in the loan consolidation program—a straight line, or constant, monthly repayment schedule, and two types of graduated repayment schedules. The repayment periods for consolidated loans are generally longer than for the original loans and monthly payments are often substantially less than those for the original loans.

Sallie Mae estimates that the consolidation program will cost the Federal Government an additional $2 million, or 5 percent, for every $100 million of loans consolidated. The additional costs would be spread over the life of the consolidated loans, which currently averages about 13 years. The estimated cost increase is based on the expectation that the added special allowance payments resulting from extended repayment periods will exceed savings resulting

from fewer defaults. The cost estimates can change with variations in a number of factors affecting special allowances including Treasury bill yields that are the basis for setting special allowances:

Volume of consolidated NDSL's, that is, national direct student loans, which are not eligible for special allowances until they are consolidated; and

Aggregate borrower indebtedness which affects the length of the repayment periods and thus special allowance payments.

Because the program has been operating for only about 1 year, it is too early to assess the program's impact on loan defaults. The annual default rate for the GSL program is 10 percent of the outstanding loan value and for the NDSL program, it is 11 percent.

Department of Education and State student loan program officials expect the consolidation program to reduce defaults.

We reviewed the potential legislative modifications to Sallie Mae's loan consolidation program in terms of four issues:

One, extending loan consolidation authority to States; two, determining individual loan interest rates by averaging the rates of the loans being consolidated; three, revising or eliminating the aggregate qualifying loan balance requirements; and four, limiting special allowance payments to the consolidated loans that were eligible for the allowance prior to consolidation.

We identified 33 programs within the States with secondary market or direct student loan authority. These programs would be the most likely to participate in loan consolidations. We contacted officials of the 33 programs, and 20 indicated that their programs would participate in the loan consolidation program if authority was extended to the States. We visited 8 of the 20 programs to obtain additional information on their interest and on their capability to administer consolidated loans.

Six had issued tax-exempt bonds to fund their secondary market and direct loan programs. One was considering issuing such bonds and the other used State pension funds to finance its operations but had authority to issue bonds. Recent bond issues by the programs have ranged from $92 million to $140 million, and in early 1983 the outstanding bonds totaled about $800 million.

A preliminary estimate provided by Sallie Mae indicates a potential nationwide market for loan consolidations of between $300 million and $500 million, and $300 million in new consolidations annually after a few years.

Using the assumption that demand for loan consolidation would be related to outstanding GSL's, we computed each State's percentage share of total outstanding GSL's at September 30, 1982. We estimate that potential consolidations for the eight States would range from about $3 million to $51 million and total about $140 million.

Because these ranges are well within the ranges of recent bond issues by the State programs we visited, it appears the programs could raise the funds needed to consolidate loans.

All of the State programs we visited used automated systems to service student loans, and according to officials of the programs, their functions for servicing, purchasing, and making student loans are similar to those required to consolidate loans. Any modifica-

tions to allow for extended repayment periods could be readily implemented.

None of the State programs offer borrowers graduated repayment schedules—options that have been selected by about 75 percent of those who obtained consolidated loans from Sallie Mae. However, each of the programs expressed the opinion that the technical expertise to develop and implement such options is available.

Whether the functions involved in the State secondary market or direct loan activities are similar to those required for loan consolidation is, according to Sallie Mae, questionable. In any event, on the basis of our discussions with the State programs and Sallie Mae, it would seem that the programs could obtain the administrative and technical capability to operate a loan consolidation program.

We attempted to estimate the potential net impact on Federal costs of extending loan consolidation authority to States. We were unable to come up with anything near a precise figure because of the difficulty in obtaining reliable information on several of the elements needed to compute relative costs. There is a cost factor that would need to be addressed, however, if consolidation authority is extended to the States; that is, the administrative cost allowance on GSL's that would be paid to the State guaranty agency by the Department of Education. Since the Federal Government has already paid the 1-percent administrative cost on the face value of the original loans, the desirability of having the Government pay a second fee for the consolidation of these same loans is something the Congress may wish to consider.

State program officials agreed that if consolidation authority is extended, criteria should be established to insure borrowers full access to consolidations and to limit repayment periods based on aggregate loan amounts.

According to officials of three of the State programs we visited, if consolidation authority is extended some State guaranty agencies may be unwilling to insure loans offered for consolidation which were originally insured by another guarantor because they did not receive insurance fees on the original loans.

Officials of all the programs indicated that requirements should be established to insure that borrowers are able to consolidate all eligible loans with a participating program. In those instances when a guaranty agency is unwilling to insure all of a borrower's eligible loans, the Department of Education could offer to insure the loans directly as it now does with Sallie Mae.

With regard to loan repayment periods according to Sallie Mae and Department of Education officials such limits are needed to prevent unreasonable increases in special allowance payments which could result if borrowers with relatively low loan amounts could extend repayment periods up to the 20-year maximum. State program officials agreed.

Both Sallie Mae and officials of most State programs we visited indicated that their programs have or could acquire the capability to determine consolidated loan interest rates by averaging, on a weighted basis, the interest rates of the underlying loans. However, Sallie Mae and Department of Education officials stated that such a modification would cause administrative problems with the spe-

cial allowance billing process and limit the Department's ability to assure itself that lenders' billings are accurate.

According to Sallie Mae, 93 percent of their consolidated loans through December 1982 were GSL's and 7 percent were NDSL's. The average weighted interest rate was 6.7 percent. At this rate, Federal costs on a consolidated loan volume of $100 million would increase by about $300,000, or about 4 percent, in the first year, and by $2.9 million, or about 5 percent, over the life of the loans. The modification would be likely to induce more borrowers to consolidate NDSL's, but we cannot estimate how much.

Determining consolidated loan interest rates by averaging the original loan rates would decrease special allowances associated with 9 percent GSL's because these loans are now consolidated at 7 percent. Sallie Mae and the Department of Education favor a change to prevent borrowers from receiving windfall interest rate reductions by consolidating 9 percent loans at 7 percent.

To qualify for consolidated loan borrowers must have loans totaling more than $5,000 from more than one lender, or totaling more than $7,500 from one lender. While borrowers with more than $7,500 can choose extended repayment periods, those with less are limited to the same 10-year maximum as provided for GSL's. However, the monthly payments to Sallie Mae by a borrower with less than $7,500 will usually be lower than they would have been without consolidation because, due to loan servicing costs, each of the original lenders would usually require at least the $50 minimum payment provided for GSL's.

The $5,000 qualifying level is approximately consistent with the current GSL requirements that provide for a minimum monthly repayment of $50 and a maximum term of 10 years. Providing more liberal repayment terms to lower indebtedness borrowers by eliminating or reducing the qualifying amounts would increase Federal special allowance payments.

Officials at most of the eight State programs we visited agreed that minimum qualifying criteria is needed to prevent excessive increases in special allowance payments.

Because the total monthly payments of borrowers with multiple loans who do not qualify for consolidation can be inordinately high because of lenders' minimum payment requirements, several States had established procedures to alleviate the burden.

I would like to point out that relatively few borrowers with lower indebtedness levels have chosen to consolidate their loans. Of the consolidated loans made through December 1982, about 13 percent were less than $8,000, and about 71 percent were greater than $10,000.

We do not believe the current qualifying loan amounts are unreasonable. If the specific levels are eliminated, one way to limit Federal costs would be to require a minimum monthly payment similar to that in the GSL program.

The last point we were to deal with was limiting special allowances on consolidation loans. While lending institutions are not eligible for Federal special allowances on the original NDSL's, Sallie Mae receives such allowances when the loans are consolidated.

Sallie Mae estimates that by eliminating Federal special allowances on the NDSL portion of consolidated loans, the allowances

paid on a $100 million consolidated loan portfolio would decrease by $500,000 in the first year and by $4.3 million over the life of the loans.

According to Sallie Mae and Department of Education officials, there are certain benefits to the Federal Government of consolidating NDSL's which should be considered when assessing the equity of paying special allowances on these loan amounts, including probable reduction of NDSL defaults and reduced Federal contributions needed to replenish college revolving funds as a result of early repayment of NDSL's.

While paying special allowances on the NDSL portion of consolidated loans may be inequitable to the Federal Government, officials of the eight State programs we visited indicated that eliminating such payments would give State programs little incentive to consolidate these loans. The officials pointed out that the cost of money and operating expenses associated with consolidating NDSL's would probably exceed borrower interest payments, in which case they would not be willing to accept the loans.

Thus, if special allowances are eliminated on the NDSL portion of consolidated loans and borrower interest rates are not increased to compensate for the lost Federal payments, borrowers may be unable to consolidate all of their loans. Of the 5,473 borrowers who consolidated their loans through December 1982, 1,601 included NDSL loans totaling $5 million. If NDSL's were not eligible for consolidation, 442 of these borrowers would not have qualified for loan consolidation.

Messrs. Chairmen, this concludes my statement. We will be happy to answer any questions you or members of your subcommittees may have.

[Prepared statement of Morton E. Henig follows:]

PREPARED STATEMENT OF MORTON E. HENIG, SENIOR ASSOCIATE DIRECTOR, HUMAN RESOURCES DIVISION, U.S. GENERAL ACCOUNTING OFFICE

Messrs. Chairmen and members of the subcommittee, we are pleased to be here today to discuss the information you requested us to develop concerning the Student Loan Marketing Association's (Sallie Mae's) loan consolidation program. Specifically, we were requested to develop information on program costs and the program's impact on defaults, and on potential legislative modifications affecting program expansion, interest rates, minimum loan amounts, and interest subsidies.

BACKGROUND

Sallie Mae is authorized by the Education Amendments of 1980 to make new loans and extend the repayment terms of Guaranteed Student Loans (GSL's) and National Direct Student Loans (NDSL's) to borrowers whose aggregate indebtedness exceeds $5,000 from more than one lender, loan program, or guarantor, or exceeds $7,500 from one lender. The act sets the interest rate on consolidate loans at 7 percent. Sallie Mae is paid a special allowance by the Federal Government on the full amount of the loans to compensate for the difference between market and consolidated loan interest rates.

The loan consolidation program is intended to reduce a borrower's repayment burden by providing extended repayment periods and lower monthly payments on relatively high student loan indebtedness. Repayment terms jointly developed by Sallie Mae and the Department of Education can vary from 10 years for loans of up to $7,500 to 20 years for loans totaling more than $16,000. Under the act, only Sallie Mae can provide consolidated loans to student loan borrowers. Sallie Mae is a private for-profit corporation created in 1972 to provide liquidity for student loans by providing a secondary market and related activities for lenders participating in insured student loan programs.

Sallie Mae began consolidating student loans in November 1981, and by December 31, 1982, had consolidated 10,648 loans totaling $66.9 million from 5,473 borrowers. Of these loans, 8,624 totaling $61.9 million were GSL's and 2,024 totaling $5 million were NDSL's. The consolidated loans averaged $12,232. The GSL's that were consolidated averaged $7,179 and the NDSL's averaged $2,488. About 70 percent of the consolidated loans exceeded $10,000. By April 1983, loans consolidated by Sallie Mae had reached $107 million.

Sallie Mae offers three repayment options to borrowers participating in the loan consolidation program—a straight line, or constant, monthly repayment schedule, and two types of graduated repayment schedules where by initial monthly payments are significantly lower than the straight line option but increase every 24 months. However, while repayment periods depend on the aggregate loan amount, the repayment periods for consolidated loans are generally longer than for the original loans and monthly payments are often substantially less than those for the original loans. For example, borrowers with aggregate indebtedness between $11,000 and $16,000 can elect to repay the loan over a period up to 16 years, rather than the 10 year maximum permitted by the GSL and NDSL programs. Typically, a borrower in this range would pay $166 monthly under the original loans and $96 monthly if the loans are consolidated—an average monthly reduction of $70.

COSTS OF CONSOLIDATED LOAN PROGRAM AND ITS IMPACT ON DEFAULTS

Sallie Mae estimates that the consolidation program will cost the Federal Government an additional $2 million, or 5 percent, for every $100 million of loans consolidated. The additional costs would be spread over the life of the consolidated loans, which currently averages about 13 years.

The estimated increase in costs is based on several assumptions. Sallie Mae's estimate assumes that investors incur no expenses associated with the purchases of Sallie Mae securities which are to provide funds for consolidated loans, and therefore pay Federal income taxes on the full amount of interest earned. To the extent that investors' expenses reduce taxable income, Sallie Mae's estimate of Federal costs for the program would increase. The estimated cost increase is also based on the expectation that the added special allowance payments resulting from extended repayment periods will exceed savings resulting from fewer defaults. Sallie Mae used a 2 percent default rate for consolidated loans in its estimate of total program costs, a figure they believe is conservative. The cost estimates can change with variations in a number of factors affecting special allowances including, Treasury Bill yields that are the basis for setting special allowances which rise or fall with changes in the yields; volume of consolidated NDSLs which are not eligible for special allowances until they are consolidated; and aggregate borrower indebtedness which affects the length of the repayment periods and thus special allowance payments.

With respect to Sallie Mae's default experience, as of December 1982, three consolidated loans totalling about $32,000 went into default—less that one-tenth of one percent of Sallie Mae's consolidated loan portfolio of about $66.9 million at that time. However, because the program has been operating for only about one year, it is too early to assess the program's impact on loan defaults. The annual default rate for the GSL program is 10 percent of the outstanding loan value and for the NDSL program it is 11 percent.

Department of Education and State student loan program officials expect the consolidation program to reduce defaults. However, a Department official indicated it would be misleading to compare consolidation default rates with GSL and NDSL default rates because default rates tend to decline as the level of borrower indebtedness increases. According to a 1982 study prepared for the National Commission on Student Financial Assistance, borrowers with cumulative GSL debts of over $9,000—the cumulative debt of most borrowers at the time of repayment is less than $3,000—default less often than borrowers with smaller loan amounts.

ASSESSMENT OF PROGRAM ALTERNATIVES

We received the potential legislative modifications to Sallie Mae's loan consolidation program in terms of four issues: (1) extending loan consolidation authority to States, (2) determining individual loan interest rates by averaging the rates of the loans being consolidated, (3) revising or eliminating the aggregate qualifying loan balance requirements, and (4) limiting special allowance payments to the consolidated loans that were eligible for the allowance prior to consolidation.

We developed information on the administrative and financial capability of State programs to administer loan consolidations, the administrative and financial capa-

bility of Sallie Mae and State programs to administer consolidations with the potential legislative modifications, and the impact of the potential legislative modifications on Federal costs.

Extending loan consolidation authority to State programs

With the assistance of the National Council of Higher Education Loan Programs, Inc., we identified 33 programs with the States with secondary market or direct student loan authority. According to a council official, these programs would be the most likely to participate in loan consolidations because they have established funding mechanisms and the authority to buy, sell, and/or make student loans. We contacted officials of the 33 programs by phone to determine their interest in participating in the student loan consolidation program. Officials from 20 of the State programs indicated that their programs would participate in the loan consolidation program if authority was extended to the States. We visited 8 of the 20 State programs to obtain additional information on their interest in the consolidation program and on their programs' administrative and financial capability to administer consolidated loans. These 8 programs provide a balance in terms of loan volume, funding levels, and geographic locations.

We sent letters to the remaining 12 programs requesting similar information, and received responses from four. Because the information they provided was more general than we were able to obtain through personal discussions, their response are not included in our analysis. However, they generally agreed with the views expressed by officials of the 8 programs we visited.

Six of the eight programs visited had issued tax-exempt bonds to fund their secondary market and direct loan programs. Of the remaining two, one was considering issuing such bonds to fund a secondary market program which had been authorized but not yet implemented, and the other used state pension funds to finance its operations but had authority to issue bonds if necessary to met funding requirements. Recent bond issues by the programs have ranged from $92 million to $140 million, and in early 1983 the outstanding bonds totalled about $800 million. Officials from each of the programs we visited believed that necessary funds could be raised to meet demand for loan consolidations.

According to Department of Education and State program officials, adequate information is not readily available to identify borrowers who are eligible for loan consolidation in order to develop accurate estimates of the potential volume of loans that would be consolidated. However, a preliminary estimate provided by Sallie Mae indicates a potential nationwide market for loan consolidations of between $300 million and $500 million, and $300 million in new consolidations annually after a few years.

Using the assumption that demand for loan consolidation would be related to outstanding GSL's because they comprised over 90 percent of the consolidations, we computed each State's percentage share of total outstanding GSL's at September 30, 1982. By applying the percentages to the preliminary market estimates, we estimate that potential consolidations for the eight States, based on Sallie Mae's lower nationwide estimate of $300 million, range from about $3 million to about $31 million and total about $84 million. At Sallie Mae's higher estimate of $500 million, the range would be about $4 million to $51 million and total $140 million.

Because these ranges are well within the ranges of recent bond issues by the State programs we visited, it appears that—as State officials indicated—the programs could raise the funds needed to consolidate loans. In any event, borrowers encountering unanticipated funding limitations at the State programs could consolidate their loans with Sallie Mae.

All of the State programs we visited used automated systems to service student loans. Four had developed their own systems and four contracted with organizations that had student loan processing systems available to interested servicers. These systems maintain demographic and loan history data, provide for merging multiple loans to establish single monthly payments over terms based on loan amounts, generate monthly billings, account for collections, initiate delinquency followup actions, and produce information needed to prepare special allowance billings to the Department of Education.

Of the eight State programs we visited: four operated secondary markets whereby they purchased student loans from lenders to improve lender liquidity; two operated direct loan programs under which loans were made to students who otherwise could not obtain them; one operated both a secondary market and direct loan program; and one had the authority to operate a secondary market but had not exercised it. In addition to servicing the loans in their portfolios, four of these programs had contracts to service GSL's in Sallie Mae's secondary market portfolio.

According to officials of the eight State programs, their program functions for servicing, purchasing, and making student loans are similar to those required to consolidate loans, and any modifications to allow for extended repayment periods could be readily implemented. The officials pointed out that: Their practice of merging borrowers' multiple loans (many students receive more than one loan during their education) to provide a single monthly repayment over periods which vary with loan amounts is a form of consolidation similar to that practiced by Sallie Mae; and their secondary market and direct loan activities involve procedures similar to those needed to consolidate loans whereby loan payoff amounts are obtained, checks are prepared and forwarded to lenders to repay student loans, and new loans are established.

None of the State programs offer borrowers graduated repayment schedules—options that have been selected by about 75 percent of those who obtained consolidated loans from Sallie Mae. However, each of the programs expressed the opinion that the technical expertise to develop and implement such options is available. On the other hand, an official observed that if states did not offer graduated repayment schedules—which would generally increase borrower interest costs and Federal special allowance payments—students wanting graduated repayments could obtain consolidated loans from Sallie Mae.

Whether the functions involved in the State secondary market or direct loan activities are similar to those required for loan consolidation is, according to Sallie Mae, questionable. In any event, on the basis of our discussions with the State programs and Sallie Mae, it would seem that the programs could obtain the administrative and technical capability to operate a loan consolidation program.

We attempted to estimate the potential net impact on Federal costs of extending loan consolidation authority to States. We were unable to come up with anything near a precise figure because of the difficulty in obtaining reliable information on several of the elements needed to compute relative costs. There is a cost factor that would need to be addressed, however, if consolidation authority is extended to the States; that is, the administrative cost allowance on GSL's that would be paid to the State guaranty agency by the Department of Education. Since the Federal Government has already paid the 1 percent administrative cost on the face value of the original loans, the desirability of having the Government pay a second fee for the consolidation of these same loans is something the Congress may wish to consider.

State program officials agreed that if consolidation authority is extended, criteria should be established to ensure borrowers full access to consolidations and to limit repayment periods based on aggregate loan amounts.

According to officials of three of the State programs we visited, if consolidation authority is extended some State guaranty agencies may be unwilling to insure loans offered for consolidation which were originally insured by another guarantor because they did not receive insurance fees on the original loans. Of the $66.9 million of loans consolidated by Sallie Mae through December 1982, $33.4 million (49.9 percent) were made with borrowers consolidating multiple loans insured by more than one guarantor.

Officials of all the programs indicated that requirements should be established to ensure that borrowers are able to consolidate all eligible loans with a participating program. An official of one program suggested that participating programs offer consolidation only to those borrowers who obtained at least one of the original loans in that program's jurisdiction. In those instances when a guaranty agency is unwilling to insure all of a borrower's eligible loans, the Department of Education could offer to insure the loans directly as it now does with Sallie Mae.

With regard to loan repayment periods based on aggregate loan amounts, according to Sallie Mae and Department of Education officials such limits are needed to prevent unreasonable increases in special allowance payments which could result if borrowers with relatively low loan amounts could extend repayment periods up to the 20-year maximum. State program officials agreed with this.

Averaging interest rates

Because all consolidated loans made by Sallie Mae currently carry a 7-percent interest rate, borrowers who consolidate NDSL loans made at 3, 4, or 5 percent experience an interest rate increase, while those who consolidate 3-percent GSL loans experience a decrease.

Both Sallie Mae and officials of most State programs we visited indicated that their programs have or could acquire the capability to determine consolidated loan interest rates by averaging, on a weighted basis, the interest rates of the underlying loans. However, Sallie Mae and Department of Education officials stated that such a modification would cause administrative problems with the special allowance billing

process and limit the Department's ability to assure itself that lenders' billings are accurate. Billings for special allowances are submitted to the Department quarterly for verification and payment. The loans are summarized by the statutory interest rates, and the categories would have to be expanded if consolidated loans are grouped by the average interest rates.

According to Sallie Mae, 93 percent of their consolidated loans through December 1982 were GSL's and 7 percent were NDSL's. The average weighted interest rate of the GSL's and NDSL's was 6.7 percent. At this rate, Federal costs on a consolidated loan volume of $100 million would increase by about $300,000—or about 4 percent—in the first year because special allowances will increase to make up for reduced interest payments by borrowers. Sallie Mae estimates that special allowance payments on such a portfolio would increase by $2.9 million—or about 5 percent—over the life of the loans. The modification would be likely to induce more borrowers to consolidate NDSL's, but we cannot estimate how much.

Determining consolidated loan interest rates by averaging the original loan rates would decrease special allowances associated with 9 percent GSL's because these loans are now consolidated at 7 percent. Sallie Mae and the Department of Education favor a change to prevent borrowers from receiving "windfall" interest rate reductions by consolidating 9 percent loans at 7 percent.

In addition to GSL's and NDSL's, the law authorizes Auxiliary Loans to Assist Students and Health Education Assistance Loans, which carry higher interest rates than GSL's, to be consolidated. While these loans do not now participate in the consolidation program, their consolidation would affect the weighted average interest rate of loans being consolidated and thus special allowance payments.

Revising qualifying loan amounts

As I mentioned earlier, to qualify for a consolidated loan borrowers must have loans totaling more than $5,000 from more than one lender, or totaling more than $7,500 from one lender. While borrowers with more than $7,500 can choose extended repayment periods, those with less are limited to the same 10 year maximum as provided for GSL's. However, the monthly payments to Sallie Mae by a borrower with less than $7,500 will usually be lower than they would have been without consolidation because—due to loan servicing costs—each of the original lenders would usually require at least the $50 minimum payment provided for GSL's.

The $5,000 qualifying level is approximately consistent with the current GSL requirements that provide for a minimum monthly repayment of $50 and a maximum term of 10 years. For example, a borrower would have to have loans of about $4,300 in order to pay off the principal and interest over 10 years at $50 a month. Providing more liberal repayment terms to lower indebtedness borrowers by eliminating or reducing the qualifying amounts would increase Federal special allowance payments. For example, the special allowance payments on a $4,000 consolidated loan with a 10-year repayment period would be about 14 percent greater than the allowances paid on a similar loan with a required minimum monthly repayment of $50 which would limit the repayment period to 9 years. Similarly, special allowance payments on a $3,000 consolidated loan with a 10 year repayment period would be about 84 percent greater than special allowances paid on a similar loan that would be paid off in 6 years under a minimum monthly payment requirement of $50.

Officials at most of the eight State programs we visited agreed that minimum qualifying criteria is needed to prevent excessive increases in special allowance payments. Officials of six programs indicated that the current $5,000 level is reasonable, and the other two believed the specific criteria should be dropped but that minimum loan requirements should be consistent with the repayment requirements of the GSL program of $50 per month.

Because the total monthly payments of borrowers with multiple loans who do not qualify for consolidation can be inordinately high because of lenders' minimum payment requirements, several States had established procedures to alleviate the burden. Two State programs generally require borrowers to obtain all of their loans from the same lender, which enables the lender to merge the loans at the beginning of the repayment period to provide for a single monthly repayment. Because loan servicing costs are relatively constant regardless of loan amounts, the resulting monthly payment will usually be lower than the total of the payments which would have been required by multiple lenders. Similarly, four State programs have been successful in encouraging lenders to buy loans from one another so that all of a borrower's loans are held by one lender.

While Sallie Mae accepts all eligible loans of borrowers who meet the qualifying levels, relatively few borrowers with lower indebtedness levels have chosen to consolidate their loans. Of the consolidated loans made to 5,473 borrowers through De-

cember 1982, 729—or about 13 percent—were less than $8,000, and 3,901—or about 71 percent—were greater than $10,000.

We do not believe the current qaualifying loan amounts are unreasonable, and some State programs have demonstrated that means other than reducing the levels can be developed to prevent high payment burdens of borrowers with low indebtedness obtained from multiple lenders. If the specific levels are eliminated, one way to limit Federal costs would be to require a minimum monthly payment similar to that in the GSL program.

Limiting special allowances on consolidation loans

NDSL loans are made by educational institutions and are funded in part by the institution (10 percent) and in part by the Department of Education (90 percent). The interest rate on these loans was 3 percent prior to 1980, 4 percent in 1980, and is currently 5 percent. While lending institutions are not eligible for Federal special allowances on the original NDSL's, Sallie Mae receives such allowances when the loans are consolidated.

Based on past experience, Sallie Mae estimates that by eliminating Federal special allowances on the NDSL portion of consolidated loans, the allowances paid on a $100 million consolidated loan portfolio would decrease by $500,000 in the first year and by $4.3 million over the life of the loans. If original loan interest rates were averaged and special allowances on the NDSL portion were eliminated, the savings would be about $200,000 in the first year and about $1.6 million over the life of the loans.

According to Sallie Mae and Department of Education officials, there are certain benefits to the Federal Government of consolidating NDSL's which should be considered when assessing the equity of paying special allowances on these loan amounts, including probable reduction of NDSL defaults and reduced Federal contributions needed to replenish college revolving funds as a result of early repayment of NDSL's.

While paying special allowances on the NDSL portion of consolidated loans may be inequitable to the Federal Government, officials of the eight State programs we visited indicated that eliminating such payments would give State programs little incentive to consolidate these loans. The officials pointed out that the cost of money and operating expenses associated with consolidating NDSL's would probably exceed borrower interest payments, in which case they would not be willing to accept the loans.

Thus, if special allowances are eliminated on the NDSL portion of consolidated loans and borrower interest rates are not increased to compensate for the lost Federal payments, borrowers may be unable to consolidate all of their loans. Of the 5,473 borrowers who consolidated their loans through December 1982, 1,601 included NDSL loans totaling $5 million. If NDSL's were not eligible for consolidation, 442 of these borrowers would not have qualified for loan consolidation.

Messrs. Chairmen, this concludes my statement. We will be happy to answer any questions you or members of your Subcommittees may have.

Mr. JEFFORDS. Thank you, Mr. Henig. Excellent statement. I know you have provided us with much valuable information. I am going to have the very rare opportunity, and probably one I may never have again. That is to now provide the distinguished Senator from my State the opportunity to ask some questions. I appreciate this chance. I am very excited.

Senator STAFFORD. Thank you very much, Congressman Jeffords.

Since this is a joint hearing of the Senate Subcommittee on Education, Arts and Humanities and House Postsecondary Education Subcommittee, it gives me the opportunity to return to the side of the House where I started almost 23 years ago. I spent 10 years on this side of the Capitol, much of it in hearing rooms like this one, occupied by the House Armed Services Committee. So it is a pleasant opportunity to return to a former scene and very pleasant memories.

Mr. Henig, we appreciate the work you have put into the report you have prepared for us. As the chairman said, it is very helpful to us in understanding the problems involved in consolidation of

student loans. I might ask you at the outset, should consolidation be authorized beyond the present limit for Sallie Mae, is there anything which would compel students who have loans at 3, 4, or 5 percent rates, to go into consolidation and thereby be bumped up to a 7-percent rate?

Mr. HENIG. We found nothing which would compel a student to do so. That is up to the student, himself, to make that determination.

Senator STAFFORD. Well, I concur in that conclusion. But I appreciate your making that statement. The obvious situation probably would be that students who have 9-percent loans might wish to consolidate at the present time in view of the fact a 7-percent rate is currently the Sallie Mae rate of interest. Are we on the same track again?

Mr. HENIG. Yes; I would think that would be very natural if a student had a lot of 9-percent loans, he would try and consolidate. That hasn't happened to any large extent yet. I understand both the Department and Sallie Mae, as I said, are in favor of changing that situation, so that there wouldn't be that kind of a windfall.

Senator STAFFORD. Right. Is there any reason to expect that the number of students choosing to consolidate their loans would increase substantially if States were allowed to consolidate on the same terms as Sallie Mae?

Mr. HENIG. There is nothing that we found that would indicate a large increase, because State agencies had the same authority Sallie Mae did. Sallie Mae made an estimate of what the probable market would be. That would be the same market whether the State agencies were involved, or just Sallie Mae.

Senator STAFFORD. Is there any reason to expect that Federal costs would be increased as a result of extending consolidation authority to State agencies?

Mr. HENIG. Senator, that is where we had our big problem of trying to figure out what the additional costs, or what the comparative costs would be. The State agencies would not get the full special allowance payment, so that would be a saving to the Government. By the same token the States now use tax-free bonds to finance their programs. That is a loss to the Government to the extent that money is money that might otherwise be invested in taxable-type information. But because we could not really get a good handle on what the additional amounts that would be borrowed by the States would be, it would be hard to estimate what the additional loss to the Treasury would be.

Senator STAFFORD. After reviewing the current consolidation program, what would be the elements in your mind of a cost effective program of loan consolidation, assuming you have some thoughts on it?

Mr. HENIG. Well, the existing program according to Sallie Mae would not, as Sallie Mae operates it would not be that terribly costly to the Government if the default rates are reduced to where Sallie Mae believes they would be. I indicated earlier Sallie Mae figures the program would cost about $2 million over the life of the program for each $100,000 in a portfolio. Their estimate is based on a default rate going down to about 2 percent. Their present default

experience is very much lower than that, considerably lower than that.

But as I said, it is too early to tell. Whether that default rate will go down or stay that low under a long-term basis, that is a questionable thing. It is hard for us to forecast. If you add some of the other features we discussed in my testimony, they would add costs to the present program. Some things would decrease costs. So I can't say what the best type of a program is. I think that would have to be based on an assessment of all the information we have developed. There are other factors besides cost which would generate interest in changing the program.

Senator STAFFORD. Thank you very much, Mr. Henig. I think before I yield to the microphone that I would just like to note for the record that in a sense this joint hearing of the House-Senate Committees on Education is unusual in the fact that both committees temporarily at least are headed by representatives from the State of Vermont and not only from the State of Vermont but from the same hometown and who grew up maybe a couple hundred yards apart from each other.

Mr. JEFFORDS. That is a good trend. I hope we can keep it up. Mr. Harrison.

Mr. HARRISON. Thank you, Mr. Chairman. I think Vermont has a majority of those present.

Mr. Henig, I guess just to summarize, if I understand what you said to Senator Stafford, it really isn't possible to estimate what would be the loss in revenues to the Federal Government if the States were allowed to consolidate. Is that a fair summary?

Mr. HENIG. Yes; part of our dilemma is this. The States presently have something over $4 billion in tax-free bonds out, something like $4.5 billion, perhaps. There is only about $2.5 billion as far as our present data show of loans purchased with that money. So there is about a $2 billion float out there that hasn't been used to purchase student loans under their existing programs. That would seem to be plenty of money to use for consolidations, so if you don't float any more bonds, you are hurting no more.

But if the States do go out and float some more tax-free bonds, then the Treasury is hurt to some extent. Another factor is, how much of that money would come from existing investors who invest in tax-free bonds. How much of that money would come from investors switching from taxable to tax-free bonds? Those are figures we can't get any real good information on, so it is hard to figure out what the additional cost would be. That is our dilemma.

Mr. HARRISON. There seems to be a similar difficulty in the sense that you anticipate that consolidation would lead to a saving by reducing the default rate, but you are not able to pin that down very precisely, either.

Mr. HENIG. No. Sallie Mae's estimate of 2 percent may be pretty good. It may be a lot lower than that. At this point it is only an estimate and we don't have any experience under a consolidation program that bears that out. We do know the larger the loan the less likely it is for default. The default rates are higher as the loan amount is smaller. And Sallie Mae is dealing with larger loan amounts, so it would tend to have a lower default rate anyhow.

Mr. HARRISON. Very good. Thank you, sir.

Mr. JEFFORDS. Senator Stafford.

Senator STAFFORD. Thank you. I would ask unanimous consent, Mr. Chairman, that an opening statement that I had intended to deliver had the vote on MX not forced me to be arriving here slightly tardily, be placed in the record along with that of Chairman Paul Simon at the opening of the hearing.

Mr. JEFFORDS. Without objection so ordered.

Mr. Petri.

Mr. PETRI. Thank you.

I would like to thank you for your report. I guess, trying to summarize in a sentence or two what you have found, tell me if this is accurate or inaccurate. The program costs are really moderate. It helps on defaults, rather than hurting on defaults, which is a plus. And there is a problem on interest rates being changed so as to avoid a windfall. One thing I am curious about, if you can speculate at all, and maybe you can't, is that as I understand it, currently about 75 percent of the people who consolidate are opting for a graduated repayment option, and is there any reason for that?

Mr. HENIG. I would speculate, I suppose you could ask the question to Mr. Fox when he testifies in a few weeks, he may have better information, but I would think that the lower the repayment period—or the lower amount of repayment in the early years, seems to fit well with most people's earnings capacity. You usually, coming out of school, earn a lot less in the first couple of years than you will later on, so that most people would seem to opt for that type of a repayment schedule.

It is the same thing with a lot of mortgages which were made available several years ago when interest rates were very high in order to induce people to buy homes, the banks were using a graduated rate which got people in at the early years.

Mr. PETRI. If you could offer an opinion, would you think it might be feasible to set up some sort of an income sensitive system of repayment directly, so you could go up and down on the individual payment rather than having——

Mr. HENIG. I think you are asking me to speculate on something which is beyond the scope of this job. I could probably give you a personal opinion, but I would prefer not to.

Mr. PETRI. OK.

Mr. JEFFORDS. Did you have any evidence which would indicate that those that are consolidating are those that probably would not be likely to default, anyway?

Mr. HENIG. The only evidence we have that this is likely is the fact that the loan default rate is less as the amount of the indebtedness is higher. There seems to be a relationship between defaults and the amount of the indebtedness. So to the extent that Sallie Mae is consolidating loans which average over $10,000, and if $10,000 has a lower default rate than say $3,000 or $4,000, yes, the default rate will come down.

Mr. JEFFORDS. Whatever conclusions you could draw from that.

Mr. HENIG. Pardon!

Mr. JEFFORDS. I said whatever conclusions you could draw from that. Thank you.

Did you make any effort to ascertain whether the existence of the loan consolidation program encouraged any students who con-

solidate from going on to graduate schools? Did you have any information on that?

Mr. HENIG. No, sir, we don't. We did not interview any students or that type of thing.

Mr. JEFFORDS. Is there any information statistically available which would tell the number of students who consolidated for the purpose of going on to graduate school, or immediately thereafter?

Mr. HENIG. No; we don't have any information like that, Mr. Jeffords.

Mr. JEFFORDS. Presently, many observers are concerned that GSL's are not always available to borrowers either seeking a small GSL or who have enrolled in short-term educational programs. Do you believe extending loan consolidation authority will encourage them to make small GSL's available in that their average portfolio size would increase?

Mr. HENIG. I can't venture an opinion on that. It would be speculation on my part to assume what a bank would do if, or State guaranty agency or lending agency might do.

Mr. JEFFORDS. You didn't see any evidence?

Mr. HENIG. No, sir.

Mr. JEFFORDS. Any other questions?

Mr. HARRISON. Mr. Chairman, I just have one.

Mr. JEFFORDS. Certainly, Mr. Harrison.

Mr. HARRISON. Mr. Henig, if the Congress were to extend the loan consolidation authority from August 1, 1983, where it is at now, to say August 1, 1985, and if we were to permit the States and other commercial lenders, as well as Sallie Mae, to consolidate student loans, do you think as a result of that GAO would be in a better position to answer some of the cost questions?

Mr. HENIG. Oh, yes. We would have some better experience to analyze at the end of a 2-, 3-year period than we have now.

Mr. HARRISON. Very good. Thank you, sir.

Mr. JEFFORDS. Thank you very much. Very, very worthwhile study and it will be very valuable to the committee. I appreciate your efforts.

Mr. HENIG. Thank you, sir.

Mr. JEFFORDS. Next in order, to complete the Vermont scenario, we have here—Senator, I want to ask as our next witness Hon. Edward Elmendorf, Assistant Secretary for Postsecondary Education, to come forward.

He came down here from Vermont in order to get things under control, and I understand has done a super job in doing that.

It is a pleasure to have you here to give us some further Vermont flavor to our testimony today.

STATEMENT OF EDWARD ELMENDORF, ASSISTANT SECRETARY FOR POSTSECONDARY EDUCATION, DEPARTMENT OF EDUCATION, ACCOMPANIED BY DAVID C. BAYER, CHIEF, GUARANTEED STUDENT LOAN BRANCH, OFFICE OF STUDENT FINANCIAL ASSISTANCE

Mr. ELMENDORF. Thank you, Mr. Chairman.

Mr. JEFFORDS. Please proceed.

I would add to that, of course, Vermont I think has more postsecondary students per capita than any other State, so here is some reason why we have a rather deep and abiding interest in the college educations. It is a pleasure having you here.

Mr. ELMENDORF. Thank you, Mr. Chairman. Would you take my statement for the record?

Mr. JEFFORDS. Certainly will.

Mr. ELMENDORF. Fine. I will try to summarize in about 5 or 6 minutes.

Let me first begin by saying that I do enjoy the opportunity to be here, especially when I have two colleague Vermonters to address some of these concerns to, because I know they are concerns that students have, as well as the Federal Government, particularly as it relates to cost. In the area of loan consolidation I think it would be helpful to cite the purpose of the program. It is a very simple statement. It is to help students who have large loan debts to try to reduce the monthly payments and try to avoid defaults that might result as a consequence.

We believe, however, that this can be done without further subsidizing interest costs. That is one of our major points today. Our aim is that we, another way to say it, we do not object to loan consolidation. I would like to repeat that, we do not object to loan consolidation. But we do oppose the proposal now written and before the committee primarily because of the unwarranted increases in Federal interest subsidy costs for educational loans. I would like to get into that as part of my statement.

It is our understanding that in the conference report of the Sallie Mae technical amendments of 1982 there was a requirement that a GAO report be delivered and discussed, and that is what we have just heard. I would be happy to have Mr. Bayer, who, on my left, is the Chief of the Guaranteed Student Loan Branch for the Department of Education, Office of Student Financial Aid.

We would like to respond to the comments we have just heard, but I would also like to add some other information from our sources that we think might help the committees. The concluding summary statement I would make is that we do plan to develop a loan consolidation authority proposal and submit it to the Congress for consideration before the expiration of the current law.

Specifically, as relates to my testimony, I would like to talk about two problems, and they are major problems. One is a problem with administration of the program, and the other focuses on some of the cost issues. Within the Department, we see as a major problem the interest rate confusion aspects of the proposal. Under the law, there is a 7-percent maximum which is fixed, but the statute that we live with also refers to the possibility of an 8-percent loan in certain cases where you have the consolidation of two 9-percent loans. That inconsistency essentially allows for an 8-percent, for the consolidation of two 9-percent loans, at the same time another provision allows for two higher interest loans like the PLUS loan, which is currently 14 percent, and the HEAL loan, which could run as high as 17 or 18 percent, to be consolidated but at 7 percent. So there is that inconsistency that I think needs to be addressed.

The impact, of course, leaving that in there in its current state, is to significantly increase the special allowance cost that in some cases aren't even being previously paid. Senator Stafford mentioned that NDSL program does not now have any subsidy. The GAO report also confirmed that. But we also note with some enthusiasm that there isn't a reason for a person with a 5-percent loan to want to consolidate at 7 percent. Still, that is left in the law at the current time.

On page 4 of the testimony we, I think, have addressed ourselves to an inequity that exists in the current law. Right now the current law, and it applies only to Sallie Mae, allows the use of a weighted average interest rate if one or more of the loans to be consolidated is a HEAL loan. This authority is not included in the proposed legislation. Unless that is changed, any extension of the authority to guarantee agencies or others would not include that provision for a weighted average.

On page 4 we try to deal with some of the technical problems that we think exist, one of which concerns us is the fact that a loan check given to a student and requiring the student's endorsement would not be traced by us back to what we consider to be the original purpose for making the loan, and that is paying off the underlying loans that have been consolidated. But giving the check directly to the student, letting them take that loan and endorse it, there is no assurance we have that the money is being used to pay back the original obligation.

Finally, in the area of departmental problems we think we have cited on page 5 some of the open-endedness in the proposal that allows for ambiguities to appear. One example I could cite is there apparently is no real authority that would disallow someone from extending the repayment beyond the 20-year possible, or to use balloon payments, or to use a schedule of graduated payment, or income contingent payment. We think that is not intended, and can be corrected with some legislative drafting.

Our second issue is the more serious one and relates to the cost issue.

Mr. JEFFORDS. Mr. Secretary, I have to interrupt you. I have to worry about another Vermont problem. We have important votes in agriculture involving the dairy industry now, and I have to get back and rescue our cows. I would just like to say, before I leave and turn this hearing over to Senator Stafford, that I am deeply concerned about your statement as to when your proposal will be ready. I would just like to urge you if at all possible to have the proposal from the administration ready before mid-June, as I anticipate this subcommittee will be marking up legislation prior to that time. I would not want to put you on notice that if it comes up as you indicated, it might be nice to look at it, but it might be too late.

Mr. ELMENDORF. I think it is possible. We would like to have the benefit of not only the GAO report but deliberations here, and any counsel we can get from Congress on it. We do have some issues that need to be decided in order for a proposal to be developed. Your counsel on that would be certainly helpful.

Mr. JEFFORDS. I appreciate that. Please proceed.

Mr. ELMENDORF. The second issue, as I mentioned before, is a much more serious one to us and it deals with some of the cost issues or problems in extending the authority. As GAO found, we, too, found it almost impossible to make any definite cost estimate due to the broad ambiguous language of the amendment as well as the substantial agency discretion that is allowed in the proposal. For example, in setting repayment terms, or other cost areas that may affect the Federal Government outlay. We have prepared some tables and charts in response to a letter from Congressman Simon that I believe is en route, and will lay out not costs for the program using current volume but will give examples of not only individual loans, consolidated versus nonconsolidated, but also assumed volumes and assumed percent showing the difference not only in the early years but the out-years as relates to the payouts by the Government.

In the area of the cost issues the extension part of the proposal will expose the Government to increased costs on the existing portfolio which is about $25 billion in total right now. That exposure comes from lengthening the repayment period from having a delay in the decline of the repayment, by adding to the GSL portfolio some non-GSL loans like NDSL's, which I mentioned, and there is a $5 billion portfolio out there in the national direct student loan, and also increasing the cost to the Government vis-a-vis the allowance for an administrative cost to guaranty agencies which is not paid currently to Sallie Mae.

There is on the other side of that some offset from default reduction. To answer Mr. Harrison's questions, we, too, find it very difficult to understand what the reduction in default might be from the availability of an options program. The average consolidation is about $12,300, and we have about $97 million in consolidated loans under the Sallie Mae program, almost 8,000 loans. And that is since the program began over a year ago. The exacerbated cost issue I think is created also by the fact that there is really in the proposal too much agency discretion which further complicates the GSL program by putting more of it outside the control of either the guaranty agency or the Government.

There is an arm's-length problem, I think, in that the law, proposed language, allows both the lender to be a lender and a guarantor at the same time. That I think is something that if we can avoid in building the legislation we ought to, so that we don't have built in potential conflict of interest.

Finally, on the revenue loss, GAO mentioned this, fiscal year 1983 Treasury estimated in communique to the Department that they assumed they had about $2.5 billion in outstanding paper and it was costing about $155 million as a result of that outstanding issue.

Later, they came back, in March 1983, with an exact estimate of $4.1 billion in outstanding tax-exempt paper. We can only assume that the revenue loss on that would be between $200 and $300 million. That is a very significant tax loss, and in our opinion, one that I think has to be addressed in any proposal that is brought forward through Congress.

A final point I would make is that I think that the legislation is unbalanced in the sense that it has concerned itself primarily with

borrower liability, but it is not sufficiently addressed what I think are some burdens that will be created on the Government from this proposal. So with that, Mr. Chairman, I conclude my summary statement and would be happy to accept your questions.

[Prepared statement of Edward Elmendorf follows:]

PREPARED STATEMENT OF DR. EDWARD ELMENDORF, ASSISTANT SECRETARY FOR POSTSECONDARY EDUCATION

Mr. Chairman and members of the subcommittee; We are delighted to have the opportunity to testify today on various aspects relating to the loan consolidation issue.

The Education Amendments of 1980 authorized the Student Loan Marketing Association (Sallie Mae) to make consolidation loans to students holding loans under the Guaranteed Student Loan (GSL), National Direct Student Loan (NDSL), Health Education Assistance Loan (HEAL) and PLUS programs if a student has loans totaling $5,000 under two or more programs or lenders or where the borrower's outstanding debt with a single lender under the GSL, NDSL, or PLUS programs is $7,500 or more. Sallie Mae has implemented this program, called OPTIONS, with the Department of Education serving as the insurer for these loans. Through March 31, 1982, Sallie Mae has made 7,870 OPTIONS loans in the amount of $97,460,197 with the average loan being $12,384.

Under current law, Sallie Mae has the authority to offer students repayment periods of up to 20 years (10 years is the maximum under other Title IV student loan programs) and provide borrowers with the option of equal or graduated repayment plans. The maximum interest rate under current law is 7 percent. We believe that this interest limitation is the major problem with the current law and the proposal. Making a new a 7-percent loan to a borrower whose underlying loans have significantly higher interest rates is not loan consolidation, it is an unwarrented increase in Federal interest subsidies.

The basic purpose behind loan consolidation is to help students with large loan debts to reduce their monthly payments and thus avoid default. We believe that this can be accomplished by extending the repayment period without further subsidizing interest costs.

Last year, the Senate considered S. 2852, which, among other provisions, would have extended the authority to make consolidation loans to guarantee agencies, State and certain private non-profit lenders. The Administration objected to this provision, due to cost considerations. The extension of the loan consolidation authority to these additional lenders and guarantee agencies was not enacted. However, as a way of assuring that the issue would be taken up this year, the Student Financial Assistance Technical Amendments Act of 1982 terminates Sallie Mae's authority to make consolidation loans on August 1, 1983. The conference report accompanying this legislation also makes clear the intent of the Congress to consider comprehensive student loan consolidation legislation, prior to that time, taking into account the recommendations of a requested GAO study. The conference report also states that the conferees felt it important to discuss this information before expanding the authority of the States or continuing Sallie Mae's authority to make consolidation loans. We wish to contribute to that discussion, and we are preparing to submit the Administration's recommendations on loan consolidation to the Congress very soon.

PROBLEMS WITH CURRENT LAW

We have identified a number of problems with section 439(o) of the Higher Education Act which provides Sallie Mae with the authority to make consolidation loans.

As previously indicated, we are still very concerned about the increase in the interest subsidies allowed under current legislation. The current legislation specifies that if a borrower has two or more 9 percent loans and the applicable interest rate for new GSL loans is 8 percent, the interest rate on the consolidation loan may not exceed 8 percent. These interest rate limitations in current law create the following anomalous situations: A student that has a single 9 percent loan would end up paying 7 percent. A student who had a 9 percent and 7 percent loan would pay 7 percent. A student who had both a 9 percent GSL and a 12 percent PLUS loan would pay 7 percent. However, a student with two 9 percent GSL's would qualify for an 8 percent consolidation loan.

Thus, the amount of special allowance paid will increase as a result of the extended repayment period. In addition, subsidies will be increased as special allowance paid increases for regular GSL and PLUS loans, and a new commitment will

be made to start paying a special allowance on NDSL's where no subsidies had been paid.

Sallie Mae's authority to make consolidation loans was altered by the Omnibus Budget Reconciliation Act of 1981 which specifies that, if one or more HEAL loans is included in the consolidation loan, the interest on the consolidation loan must be a weighted average interest rate. However, this weighted interest rate does not apply to a student who might have a 12 percent PLUS loan and thus end up with a 7 percent consolidation loan under current law. Furthermore, this provision governing Sallie Mae's consolidation of HEAL loans is not included in the proposed legislation which would extend the authority to make consolidation loans to guarantee agencies and other lenders.

Section 439(o) of the Act now provides that section 427 of the Act governs the terms of consolidation loans with two exceptions. Consolidation loans are exempt from both the 10 year repayment period and the fifteen year life of the loan limitations which apply to most guaranteed student loans. However, there are a number of other provisions in section 427 which establishes the terms of loans under the Federal Insured Student Loan Program, which are of questionable value or applicability to the loan consolidation program, but which would, as written, apply to the existing Sallie Mae loan consolidation program, and under S. 2852, to the Guarantee Agency Consolidation Programs.

Section 427 creates further problems by requiring that the loan check be made payable to the student and requiring the student's endorsement. There is no way to insure that the proceeds from consolidation loans are used to retire prior debts unless the check is made payable to and sent to the holder of underlying loans.

Another provision of the current law which especially causes us some concern states:

"Notwithstanding any other provision of this part, the Association, with the agreement of the borrower, may establish such repayment terms as it determines will promote the objectives of this subsection including, but not limited to, the establishment of graduated, income sensitive repayment schedules."

This language appears to be overly broad and would appear to authorize the lender (Sallie Mae) to disregard the statutory provisions relating to the repayment terms, such as the maximum 20 year repayment provision. We assume, the intent was to authorize flexibility within the statutory prohibitions. While there has been no indication that there are problems with Sallie Mae regarding this provision, if the program is extended to a significant number of new lenders, this could present significant problems, especially with regard to increased costs to the Federal Government for special allowance payments. For example, it appears lenders could begin authorizing repayment periods longer than 20 years or authorize limited periodic payments with a "balloon" payment at the end of the repayment period.

EXTENDING CONSOLIDATION

We are concerned about the proposal to extend loan consolidation authority to the guarantee agencies and other direct lending authorities as it will further expose the Federal Government to increased costs on the existing portfolio.

In general, loan consolidation increases Federal subsidy costs by lengthening the repayment period, delaying the decline of the borrower's balance, and adding to the GSL outstanding portfolio the potentially large amount of currently non-GSL loans. (There is approximately $5 billion outstanding in the NDSL program alone.) In addition, in the Senate proposal, loan consolidation also would reduce formerly 8 percent GSL's and 9 percent GSL's as well as potentially 12 and 14 percent PLUS loans and market rate HEAL loans to a 7 percent interest rate. Although NDSL loans already bear low interest (3, 4 or 5 percent) they do not require Federal interest subsidy appropriations and extending their repayment period could still lower a borrowers monthly payment even at a higher interest rate. Also the proposal creates higher "new" loan volumes under guarantee agency guarantees. This "new" consolidated volume would be the basis for increased guarantee agency Administrative Cost Allowances which requires further Federal outlays.

All of the above factors tend to increase direct Government costs. Reduced default rates due to consolidation/refinancing would be expected to off-set these increased costs to a limited extent. However, long term net default costs are extremely hard to estimate, and the impact of these new consolidation authorities on such costs are very hard to identify. We would especially like to stress the fact that the considerable agency discretion (in setting borrower repayment periods and other areas) provided in the proposed expansion amendments would place the GSLs liabilities even further out of Government control.

The Senate bill specifies that loans made by a guarantee agency under this new authority would also be insured by that guarantee agency. The lack of an "arms-length" relationship between the lender and the guarantor could present some problems, especially in the enforcement of due diligence in collection requirements. As a matter of fiscal prudence, we believe it more reasonable if the guarantor and the lender are not one and the same.

Finally, there is one more Federal cost issue which needs to be addressed. Sallie Mae obtains its funds in the marketplace and pays Federal income taxes. The interest earned by investors in Sallie Mae's obligations is taxable. However, as the proposed legislation is drafted, it would appear that many of the agencies that would be extended the authority to make consolidation loans would obtain their funds through the issuance of tax exempt obligations. The net affect would be that student loans made from the proceeds of taxable obligations would be refinanced with funds obtained from non-taxable obligations. There is major concern within the Administration about the loss of Treasury revenue resulting from tax exempt obligations issued for student loans and other purposes.

In summary, the Administration opposes the proposals now before the Committee to extend and expand the loan consolidation authority (currently limited to Sallie Mae) because they provide unwarranted increases in the Federal interest subsidy for education loans. These proposals open the door to major abuse of these programs operation and their original congressional intent. As proposed, these loan consolidation bills are not as much focused on consolidation as they are focused on reducing the interest liabilities of the borrower. We have not yet estimated the full cost of these proposals but they are substantial because any one with a 9, 12, 14 percent or market rate loan will not hesitate to consolidate them into a 7 percent loan as soon as they are able. The potential increase in interest subsidies paid by the Federal Government would be huge.

We do not object to loan consolidation. We plan to develop a loan consolidation authority that does not increase Federal interest costs and submit it to you in time for your consideration prior to the expiration of current law.

I am happy to have had this opportunity to appear before you today. I shall be happy to answer any questions that you may have.

Senator STAFFORD. Thank you very much, Dr. Elmendorf. I enjoyed listening to your testimony. I think you have pointed out some issues both sides of the Capitol need to address in considering the consolidation of loans for Sallie Mae and extending that to State agencies.

I would like to reinforce what Congressman Jeffords said earlier about the timeliness of getting the administration proposals up on the Hill. I expect the Senate is going to be in session through July according to all the tea leaves I can read at the present time, and the House also. But the August recess is now coming up on us fairly rapidly. The sooner we could have any administration proposals, the better, both for the administration and for us here on Capitol Hill.

Last year during the conference on the higher education technical amendments bill, the administration suggested that extending consolidation to States would cost, as I recall it, about $250 million. I wonder, Mr. Secretary, if you could tell us how the Department arrived at that figure, and whether or not that is still a legitimate estimate of the increased costs that might be involved.

Mr. HENIG. Mr. Chairman, I would like to turn this over to Mr. Bayer, who has some tables available to him that can, for an individual loan, show you essentially what the difference would be.

Senator STAFFORD. All right.

Mr. ELMENDORF. I must state though, again, in trying to put together any proposal, the combination of variables you have to decide on up front really do create the difference between consolidated and nonconsolidated loan packages. In most of the proposals we tried to cost out, I will say we used the 7- and 8-percent interest

rate. We tried to use a typical loan amount as being $6,000 or $7,500. We used the repayment periods that were either under current law 10 years or extended out to 15.

Finally, in trying to determine the special allowances really where the burden of the Federal Government is most directly felt, we assumed that there would be guaranty agency involvement in terms of our costing, and we mixed both the current Sallie Mae financing with half special allowance financing.

So considering just those variables, Mr. Bayer has got some numbers I think he can share relative to individual loans and some bulk loans.

Mr. BAYER. I might point out some of the problems in trying to come up with cost estimates is to try and make the assumption as to read the proposed legislation literally, or the way we assumed you meant it to read. For example, in the legislation as drafted right now the cost to the Federal Government would be very minimal because if the program were extended to guaranty agency programs, the law would not permit us to pay any special allowance to consolidation loans made by guaranty agencies.

I am not sure that was intended. So therefore we assumed that there would be guaranty agency special allowance consolidation loan costs. On a 7-percent consolidation loan, again, one of the problems is the fact that all loans must be 7 percent loans under current law, on a 7-percent loan, assuming an average loan of $7,500, repaid over a 15-year life of the loan, the costs of a consolidated loan would be about $649 more to the Federal Government than for a nonconsolidated loan paid over a 10-year period, which is the current statutory maximum repayment life of the loan.

Senator STAFFORD. Do you have the figures with you that substantiates that statement?

Mr. BAYER. Yes, sir.

Senator STAFFORD. I wonder if there would be any objection to us putting those figures in the record of this hearing so both of our subcommittees could have them.

Mr. BAYER. We will be happy to provide these four tables of statistical tables for the record.

Senator STAFFORD. The statement has been made there is a loss of Federal income if State agencies were allowed consolidation, and I have a little trouble with that because I accept the fact that Sallie Mae goes to the marketplace for borrowing funds to implement their programs, which is true. But States may get tax-free revenues from bonds, from selling bonds. They are doing that anyway. So I wonder if you could explain to me why there would be a loss of Federal tax dollars if the States were allowed consolidated loans of students.

Mr. ELMENDORF. If, Mr. Chairman, we assume Sallie Mae's projections of a $500 million loan consolidation portfolio under the options program, realistic, we take that over a 3-year period of time and look at what has happened just since tax exempts have been made available, just for this program we find that there has been almost a doubling in the amount of tax-exempt paper in the last 2 years, from $2.1 billion now to $4.2 billion.

If the ratio of climb is—without the options program full in effect, is $2 billion, and the interest rates or revenue loss that

would be paid to Treasury on that is anywhere near the $150 to $300 million, I think what we are talking about is the Treasury of the United States not having $300 million it might otherwise have if we could work a different way to consolidate these loans and extend the authority.

Senator STAFFORD. I guess my difficulty, Doctor, is I don't really understand the difference between the States consolidating loans, and borrowing tax-free money to do it, and making the loans without consolidation, then borrowing tax-free money to do that. That is the difficulty I have with that particular argument at this point.

Mr. ELMENDORF. I would have a question about where we are getting the tax-free money to borrow under the current program, because we are looking at $180 billion deficit that we are trying to make every effort to reduce. We would like to get that down to a zero sometime in the future.

Senator STAFFORD. I presume, Mr. Secretary, you may not be able to be in a position to answer this question, but let me ask it anyway. Does the administration, to your knowledge, favor loan consolidation as a matter of prudent Federal policy?

Mr. ELMENDORF. As a matter of?

Senator STAFFORD. Prudent Federal policy.

Mr. ELMENDORF. We have stated in our testimony that we do support the concept of loan consolidation, yes, sir.

Senator STAFFORD. If so, and maybe this is a premature question in view of the fact you are going to have some legislation up to us for consideration, how would you devise a cost-effective program of loan consolidation?

Mr. ELMENDORF. I knew you were going to ask that question. I would first of all safeguard the Federal Government from all of the inherent weaknesses I have cited thus far. And I would go to some issues I think need to be addressed. If I might just cite four of them I think should be tackled by at least us, and we hope by Congress as well.

Senator STAFFORD. Certainly.

Mr. ELMENDORF. We think a serious issue is what source of capital is there for consolidated loans. This addresses itself to your concern about using tax exempt, my concern, and other funds that may be available. A second concern we have deals essentially with whether that authority under 2852—S. 2852 should be extended to guaranty agencies and to certain nonprofit lenders. There is a series of issues relating to that.

We are certainly supportive of any competitive system. and if we can work out more competition, I am sure Sallie Mae in their testimony supported the notion that they do not intend to be monopolistic in their practice of being the only agent right now for the consolidation program.

The third issue I think is the interest rate. I have cited what I think some of the inequities are with that. I would like to see us deal straight up with the issue of the 7 percent, and the contradictions in the law that deal with the weighted average, and come up with an acceptable interest rate formula.

I think we also have to talk about the types of loans to be consolidated and whether or not we want to include just GSL, or GSL

and NDSL, or PLUS loan, or HEAL loan, or all the other loans out there that students are currently eligible to receive.

There is a fourth issue that deals with a loan fee of some sort. Right now, Sallie Mae consolidates and does it on the basis of a dollar per loan, and they pay the dollar. Under the proposed law, I cited that we would have an administrative cost allowance, and that could run quite—be quite an expensive outlay if it were under current law paid out to guaranty agencies. At least those four issues, with various options under each of those issues, I think, need to be addressed, and addressed rather promptly.

Senator STAFFORD. Thank you very much, Mr. Secretary.

Mr. Harrison.

Mr. HARRISON. Thank you, Mr. Chairman. It seems like you and I keep meeting at hearings. I was testifying before the Senator yesterday, and we are sitting up here together on something else today.

Mr. Secretary, I think in your testimony you mentioned a communication which you received from the Treasury Department. Would you have any objection to making that available for the record?

Mr. ELMENDORF. No, sir.

Mr. HARRISON. Second, I think in your last answer to Senator Stafford, you emphasized again the not-for-profit nature of most of the lenders. I guess the question that occurs to me is, do you think there would be any cost differential if we were to include for-profit lenders, banking institutions, as well as not-for-profit lenders in the program?

Mr. ELMENDORF. As I said, it is one of those major issues that I think needs to be addressed. If you were to open it up to commercial lenders for profit, you certainly would have on the plus side the reduction of some of the outlays that would normally go only to State guaranty agencies. On the other hand, you would want to have some assurance of a sufficient portfolio there to underwrite these loans. So I think a formula with some criteria attached to it would be appropriate to answer that response.

Mr. HARRISON. Very good. Lastly, I think you heard the gentleman from the GAO in response to a question I asked him, I guess I would like to get your reaction. What would be your reaction to an extension of the loan consolidation authority to, let us say, August 1, 1985, permitting the States, other commercial lenders, and Sallie Mae to consolidate? Do you think that that timeframe for further study would be helpful?

Mr. ELMENDORF. I would like to answer that two ways. No. 1, given the fact that we would oppose the way the law is written now, which includes in an open-ended way all of the other possible authorities, I would say we would probably oppose that unilateral extension. At this point, however, since we have the agreement with Sallie Mae which originated the options program, I don't believe we would have any objections to the continuation of the options opportunity as it is now construed into the outyears in order to study the problem further.

But we have taken seriously the concept of loan consolidation, and the concept that, if there is good reason for there to be other authorities, then those authorities ought to have the ability to com-

pete for this type of program. And that is why we are anxious to develop loan consolidation legislation that takes some of the bugs out that we think are in there, and opens the door to others.

Mr. HARRISON. In that event, then, can I just, from this side of the table, emphasize again what Mr. Jeffords and Senator Stafford have said, and that is that if the administration has a proposal, I guess the sooner it gets up here the better.

Mr. ELMENDORF. I can certainly speak for the Assistant Secretary for Postsecondary Education on his part for getting that proposal out.

Mr. HARRISON. Thank you, Mr. Secretary. Good to see you up here again.

Senator STAFFORD. Thank you, Mr. Harrison.

Mr. Petri.

Mr. PETRI. Thank you, Senator. I guess I do have a couple of questions. Am I right to say that you are not against the principles, or the idea of consolidation, but you are worried that it not be a device for increasing government expenditures without thinking it through carefully?

Mr. ELMENDORF. That is correct. The concept is certainly acceptable, the proposal as it is now construed leaves too many open doors through which we think fraud, waste, and abuse kind of opportunities can enter.

Mr. PETRI. Now, one question I had, and I don't know if you have thought of it or people have figured it out, in all the talk about the possible costs to the government of consolidation, have you calculated the possible savings to individuals and financial institutions and so on from consolidation? I don't know how much they figure a check costs and postage and everything else. There is certainly a big saving just from consolidation. We really shouldn't be looking at it purely from the point of view of the U.S. Government, but from the point of view of the whole society in calculating that.

There is some cost to the government, but there is greater savings to individuals and financial institutions and so on in paperwork and overhead. That at least is a good argument for having some small costs on the government side of the ledger.

Mr. ELMENDORF. That is a good question. And the part of it that deals with the commercial lenders or Sallie Mae, they have had experience with the program. And in their testimony I believe I read a number of citations that deal with what they consider to have been a return on profit, or in this case they like to use return on assets, which is in the corporate world a good measure of an investment.

In this particular case if you were to include in what they have done with this portfolio as they have configured it, with average loans of $12,300, there is a return on that investment that is satisfactory to keep them in the program.

From the other perspective, unless you are able to get a good grip on how many defaults which potentially would have occurred if the program hadn't been in place, you don't get a good fix on a balance between the Federal cost to continue against the actual savings by bringing someone into repayment.

Sallie Mae has a rule which I think is a rather good one that someone has to be in repayment for at least three consecutive pay-

ments before they can be eligible for the options program. That sort of says that we don't want people that are not in repayment to suddenly find this to be an easy way out of paying what is due the government. I think provisions like that thought out for Sallie Mae and other authorities are really what we need to seriously address.

Mr. PETRI. But absent everything else, I mean I as someone who graduated from school and had several loans, would be much happier, if everything else were even, just paying one check rather than three or four to different people because of the paperwork and postage. Banks charge 25 cents to $1.50 a check these days, and so on. I assume that is because it costs them. So if you just can reduce all that, that has to be a social benefit of some considerable size, if enough people do that.

Mr. ELMENDORF. Maybe Mr. Bayer would like to respond to the latter half of your question.

Mr. BAYER. I think your point is well taken, Mr. Petri. The student certainly does save an awful lot of administrative headaches and nightmares to make sure they don't forget a payment and put all the various checks in the mail they have to with multiple loans. Especially today with borrowers frequently having loans from more than one lender through more than one guaranty agency program, through more than one program itself with conflicting repayment terms and conflicting repayment requirements, it does certainly provide incentive for the borrower to have a single place to pay loans.

Finance companies for years have been making their bread and butter by arguing just this point, for making consolidation loans to consumers who have loans from a wide variety of creditors. Lenders certainly would save collection costs and other costs by having the loans converted into a single consolidation loan. To the extent you consider all the costs incurred by all the various lenders involved. Schools participating in the national direct student loan program would get their capital back a lot faster, thus able to lend it again, thus reducing the demand or need for additional Federal capital contributions.

I think there are a great many benefits of this sort that could be cited.

Mr. PETRI. Sometimes consolidation result in extending the period of repayment, and therefore, under current practices, increasing the subsidy. Have you considered having some sort of an end to that extended subsidy? That might invove having the consolidated loan balloon at the end, and the person get no subsidy or pay market rates at the end of the current subsidized period. For example, the loan might go from 7 years to 9 years' repayment, but the last 2 years would be profitable, or at least income neutral to the Government, rather than 2 more years of subsidy.

Mr. ELMENDORF. Yes. Not only that but the income contingent factor is also a part of what is already in the proposal. Under the current operation, you heard stated that 75 to 80 percent of the volume that Sallie Mae underwrites is written under a graduated payment schedule, rather than in equal payments. I am sure there is good reason for that on behalf of both the borrower and the lender. So I think those financial as well as convenient opportunities are potential and should be looked at.

Mr. PETRI. I have to ask one or two more questions here. Sallie Mae presently offers loan consolidation to students at a 7-percent interest rate. Do you believe raising this interest rate to 9 percent would discourage students needing loan consolidation from consolidating their loans?

Mr. ELMENDORF. I really would prefer not to answer that question on the basis that I couldn't answer it any better for 9 percent than I could for 12, or even 7. I have only got data on 7, and the hypothetical 8 that is in the current law. We have not done a matrix with a whole set of different interest rates and costed them out. Just what we have done between 7 and 8 from our initial table does not show a very high increase in the Federal Government of the program. But I don't know that that would be the case with a 7 to 9 jump. So I would really want to cost that out.

Mr. BAYER. It should be pointed out it is less of an advantage to a student who currently has four or five NDSL loans if the rate were changed from 7 to 9 percent. I am not sure it would be construed as an awful disadvantage to the student who has a market HEAL rate if changes from 7 to 9 or a person with a PLUS loan of 14 percent if that rate were changed to 7 or 9. That would still be a decrease if the rate were changed for the borrower.

Mr. PETRI. One point made at the hearing yesterday was that consolidations could discourage banks from making small GSL's. The concern expressed was that types of loans that would be consolidated, the larger loan portfolios, would be transferred to Sallie Mae, thus reducing the average portfolio size at the lending institutions and placing further pressure on the lender not to make small loans.

Do you agree with that analysis, or have any comment on that testimony?

Mr. ELMENDORF. No; I really couldn't say that I agree with it. But I don't have enough data to disagree with it at this point. We have not had direct consumer complaints from those that have been excluded from the program because of the insufficient size of the loan, or the inability of the lender to give small loans. There have been a lot of allegations around that this is keeping people out of the program. But my sense is that, as secondary markets become more experienced with buying portfolios and servicing them, they are learning for themselves what is profitable in terms of a cumulative number of loans that they can buy from a bank.

I think that analogy can also be applied to the cumulative number of dollars that would be advisable for a guaranty agency loan consolidation authority to want to get into. One way it may help them, by having that minimum that is now $7,500 for one source, or $5,000 for two sources, be reduced essentially.

Mr. PETRI. One final question. You are very patient. You did refer in your testimony I think to a whole series of miscellaneous, different loan programs, and that there should be some systematic examination of what should be eligible for consolidation, or what should not. I assume that is one of the things you hoped to cover in this proposed legislation.

Mr. ELMENDORF. Yes, sir.

Mr. PETRI. But in that connection, do you believe that health education assistance loans should be eligible for loan consolidation? Why, or why not? I guess maybe that is a litmus test. Are you going to be leaning in the direction of making more loans eligible for consolidation, or trying to reduce the loans that are eligible?

Mr. ELMENDORF. Well, we haven't really come to any kind of consensus on that, but my sense is that a prior question has to be addressed. That is the question about the interest rate and how it is determined. If it is a fixed rate, I might answer the question one way. If it is a weighted average I might answer it an entirely different way. And the HEAL loan benefits from the weighted average approach. We would in the Government not be advantaged if we had a fixed rate and those HEAL loans were in our scope of consolidation, because the special allowance difference that we had to pay out would be significant, and the costs would escalate. So I would answer that differently depending upon the answer to the prior question about which interest rate formula we would propose using in any new loan consolidation authority.

Mr. PETRI. So if I read you right, what you are saying is if you were not extending the subsidy, then it might be a good idea to broaden the consolidation because of the general convenience. But if you are somehow increasing the costs to the Government, then you would be very reluctant to bring more of these loans——

Mr. ELMENDORF. That is a good principle.

Mr. PETRI. Is that the one——

Mr. ELMENDORF. That is the one we are following, yes, sir.

Mr. PETRI. So you are saying if we keep the interest rate low, then you wouldn't mind having consolidation, but then you wouldn't like that low-interest rate to apply to the other loans that were brought in. They would have to be at a higher rate?

Mr. ELMENDORF. You can afford to be more magnanimous if you know that the Federal Government is not paying the cost in terms of the numbers of loans that are you allowed to be consolidated. But if your subsidy costs shoot up directly, you are going to be more in a mode of trying to confine that upward cost to the Government as much as possible.

Mr. PETRI. I think it would be useful, at least if you would think about it, figuring out some sort of cost savings to the society in general that could occur from consolidation even if there were no subsidy. In trying to sell something like that, I think everyone would agree it would be better to have consolidation as broad as possible just from the point of view of convenience for the citizenry and savings in paperwork and costs. You could nonetheless sell this as a break for people, even if it is not a direct Treasury subsidy.

Mr. ELMENDORF. I think that is a good approach.

Senator STAFFORD. Thank you very much, Mr. Petri.

Mr. Secretary, we are grateful to you for appearing in front of this joint meeting today with us and with your colleague. We again urge you to get whatever legislation the administration has to us as soon as possible, certainly before the Fourth of July recess of the two Houses, which will give us the month of July to digest them.

I guess if there is no further testimony, this joint meeting of the Senate Subcommittee on Education, Arts and Humanities and House Subcommittee on Postsecondary Education is adjourned subject to call of the joint Chairs.

[Whereupon, at 3:13 p.m., the subcommittees were adjourned, to reconvene subject to the call of the Chairs.]

STUDENT LOAN CONSOLIDATION

WEDNESDAY, JUNE 8, 1983

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON POSTSECONDARY EDUCATION,
COMMITTEE ON EDUCATION AND LABOR,
Washington, D.C.

The subcommittee met, pursuant to call, at 9:35 a.m., in room 2261, Rayburn House Office Building, Hon. Paul Simon (chairman of the subcommittee) presiding.

Members present: Representatives Simon, Andrews, Penny, Coleman, Gunderson, Petri, and Packard.

Staff present: William A. Blakey, majority counsel; John Dean, assistant minority counsel; Patricia Morrissey, minority legislative associate; and Betsy Brand, minority legislative associate.

Mr. SIMON. Good morning. The Subcommittee on Postsecondary Education today continues its hearings on student loan consolidation. Last year during congressional consideration of the student financial assistance technical amendments of 1982, the authority of the Student Loan Marketing Association, better known as "Sallie Mae," to continue consolidation of student loans was terminated, effective August 1, 1983.

Congress authorized a study of the costs and policy implication of expanding loan consolidation authority to State guarantee agencies. Recently, the General Accounting Office reported, and I am quoting now:

> We attempted to estimate the potential net impact on Federal costs of extending loan consolidation authority to States. We were unable to come up with anything near a precise figure because of the difficulty in obtaining reliable information on several of the elements needed to compute relative costs.
>
> State program officials agreed that if consolidation authority is extended, criteria should be established to insure borrowers full access to consolidations and to limit repayment periods based on aggregate loan amounts.

End of the quote.

Many of questions related to the cost of extending loan consolidation authority to State agencies and other lenders remain unanswered. I am especially concerned about the revenue implications of using tax-exempt student loan bonds to provide loan consolidation capital.

I am also concerned that a uniform set of terms and conditions be utilized by all who engage in loan consolidation in order to avoid any additional complexity in the current student loan system and a loan consolidation maze among the States. Finally, while I believe some form of loan consolidation is essential—that's too strong a word—let's make it desirable, creating additional costs in

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the student loan programs at this time is not advisable. The Federal responsibility to provide access and some measure of choice in postsecondary education for low- and middle-income students extends to students while they are students.

The principal argument supporting loan consolidation was that it would reduce defaults. In fact, loan consolidation has had a negligible impact on reducing student loan defaults. The available evidence suggests that those persons most likely to consolidate their loans are those who are best able to repay their indebtedness anyway.

This means that the objective originally sought is not necessarily being achieved and the Government's costs are increasing due to extended repayment period accorded those who use Sallie Mae's services.

I believe we should concentrate limited Federal higher education dollars on students seeking access to a quality higher education and that less attention should be directed to former students who have already benefited from these programs.

I am anxious these concerns and others expressed by our witnesses today.

We have another member who has joined us. You may have to take over here in a little while because we have some conflicts going on today.

Do the others have any opening comments here?

Mr. PACKARD. No, thank you.

Mr. SIMON. Our first witness is Edward A. Fox, president of Sallie Mae, who is getting to be a regular here these days.

STATEMENT OF EDWARD A. FOX, PRESIDENT, STUDENT LOAN MARKETING ASSOCIATION (SALLIE MAE)

Mr. FOX. Thank you, Mr. Chairman.

Your opening remarks indicate a pretty substantive knowledge of the issues so I will give you my testimony for the record and will just highlight one or two things.

Mr. SIMON. OK. Your full statement will be entered in the record.

Mr. FOX. Thank you very much.

[Prepared statement of Edward A. Fox follows:]

PREPARED STATEMENT OF EDWARD A. FOX, PRESIDENT AND CHIEF EXECUTIVE OFFICER, STUDENT LOAN MARKETING ASSOCIATION (SALLIE MAE)

Mr. Chairman, I appreciate the opportunity to testify before this Subcommittee on student loan consolidation and on Sallie Mae's OPTIONS Program. In my testimony I will review the creation of the OPTIONS Program, the complexity of the process of consolidating a student's indebtedness, the General Accounting Office (GAO) study recently submitted to the Subcommittee, and the concerns of the Department of Education that have been expressed to this Subcommittee.

The Education Amendments of 1980 authorized Sallie Mae to make consolidation loans to borrowers with federally insured or guaranteed student loans where the aggregate indebtedness from 2 or more lenders or programs exceeds $5,000, or $7,500 from a single lender, with maximum repayment periods not to exceed 20 years. Under this authority Sallie Mae has created the OPTIONS Program.

Sallie Mae's OPTIONS Program is a workable, successful concept representing substantial investment of our resources for program design and for originating and servicing capacity. We want to continue to offer this program. We leave to the Congress the policy determinations as to how many programs of loan consolidation should exist. We will endeavor to provide loan consolidation consistent with any

program you authorize. However, our greatest concern is that the structure of any program of loan consolidation you authorize take into account the complexity of the process. Sallie Mae currently provides a nationally uniform system, making the student's choices clear and understandable, and providing secure servicing capacity for these extended and graduated repayment loans. We cannot stress too strongly the advantages to the student and to the program of a uniform set of consolidation standards and uniform originating and servicing requirements for consolidated loans.

Students who receive loans under the Guaranteed Student Loan Program (GSLP) or the National Direct Student Loan (NDSL) Program may be eligible to consolidate monthly payments on several loans into one payment and to extend the length of repayment beyond the ten-year term allowable under the current GSL or NDSL Programs. Consolidated loans are guaranteed under the terms of the GSLP. Consistent with this legislative intent, Sallie Mae provides sound debt management for students through a nationwide, readily available program of loan refinancing for borrowers.

Rapidly increasing tuition and fees have dramatically increased the dependency of students on loans to finance a significant portion of postsecondary education costs. While the GSLP is the largest single source of educational loan capital, students often borrow under other programs in addition to the GSLP. Likewise, students may borrow from different GSLP lenders depending on the number of schools attended, residency, and availability of funds. In authorizing loan consolidation, Congress recognized that student borrowers could be faced with severe debt management problems due to the multiplicity of loans and the requirement of simultaneous repayment of these debts. Refinancing or consolidation of loans establishes initial repayment burdens more evenly with the borrower's current ability to repay, thereby reducing the potential for default.

Sallie Mae was designated to implement loan consolidation because of its ability to apply sound credit and lending principles to this program and because of its capability to deliver service on a nationwide basis. Development of any financial service requires a significant investment of time, money, and expertise without assurance that the product will be successful. Such an investment is justified by the potential benefits to the GSLP and to student borrowers of a sound program of loan consolidation. Further, Sallie Mae has the financial resources to invest in this program without diverting resources from primary loan availability because Sallie Mae is not a primary lender in the GSLP. As the largest holder of student loans, it has the procedural and systems support which assures the integrity of this program.

Immediately after the passage of the Education Amendments of 1980, Sallie Mae began the process of designing a workable loan consolidation system and negotiating such a system with the Department of Education which had agreed to insure the consolidated loans. This process was time consuming and complicated, but through it we were able to establish a uniform national program with terms that the Department assured were consistent with federal law and policy.

Considerable research was undertaken to determine the number of students eligible for the program because of the lack of an integrated data base. In point of fact, Mr. Chairman, we cannot tell you today how many students qualify for loan consolidation. We simply do not know.

The process, procedures, controls, and documentation had to be created for a product that never existed before. An entirely new originating and servicing system was developed. By October of 1981, the necessary systems, controls, and procedures were in place and the approval of the Secretary of Education was secured.

Sallie Mae's loan consolidation process has been designed to meet the broad set of objectives we believe intended by the federal statute. Sallie Mae's investment in a computer system and in analyses of the complexities of the process has been substantial.

The automated system which supports Sallie Mae's program was developed at significant cost. One of the dominant design objectives was to achieve consistent treatment of the many unusual conditions which give rise to the need for a consolidation loan. For this reason, the computer system is on-line and maintains a very large data base for each borrower. Further, Sallie Mae has made a major investment in documentation of all procedures and in establishing a thorough consumer lending training program.

An important advantage of the OPTIONS Program is in the graduated repayment feature. The graduated repayment module of Sallie Mae's program offers two repayment alternatives and is designed to automatically interface with the complex requirements needed to amortize a loan with graduated repayment.

Sallie Mae's automated system also provides for a significant amount of data on the demographics of borrowers who apply for consolidation. This system capability was included in recognition of the need to provide adequate program reporting to federal agencies and Congressional committees having interest in the OPTIONS use.

The extensive investment by Sallie Mae in the system and the processing controls surrounding it have produced a timely, full compliance, and consumer oriented approach to the legislative intent of the program. The shortcuts others have suggested may come about only at the sacrifice of compliance with the statute's provisions, or by reducing the amount of relief accorded the borrower, or finally, at the expense of traditional banking practices for loan origination.

Sallie Mae's knowledge of loan consolidation has come after a very concentrated effort to design and administer the best possible program. Should the number of participants in the consolidation program be increased, the same measure of care and diligence in design and implementation must be achieved. Otherwise the concepts envisioned by the original statute and confirmed by the GAO audit as provided by Sallie Mae will be lost through hastily constructed programs with widely different procedures and interpretations of compliance.

Our goal was to provide maximum participation for the borrower in selecting payment terms, both fixed repayment and graduated repayment, which could be effectively serviced but which did not present the borrower with a bewildering array of decisions. We believe we have succeeded in that effort. I have appended to my statement a copy of the information provided to the student on OPTIONS as well as other documentation which is necessary to complete the consolidation process.

We believe the experience in the Sallie Mae OPTIONS Program shows the usefulness of the concept of consolidation.

LOAN CONSOLIDATION STATISTICS THROUGH APR. 30, 1983

	Percent	
Program volume		$117.1
Borrowers		9,328.0
Average balance		$12,500.0
Average term selected (months)		171
Program mix:		
GSL	93	$108,800,000
NDSL	7	$8,200,000
Distribution of indebtedness:		
$5,000 to $7,000	10	
$7,000 to $9,000	14	
$9,000 to $15,000	52	
$15,000 and above	24	
Option selected:		
I (extended term, fixed payment)	25	
II (graduated repayment)	70	
III (accelerated, graduated repayment)	5	
Delinquency:		
30 to 60 days	1.23	
61 to 120 days	.77	
Over 120 days	.24	
Defaults: Claims in process	.13	

The loan consolidation process appears straight foward and simple:

A borrower is made aware of the program through: a Sallie Mae mailing; a financial institution mailing; a school mailing or exit interview; a guarantor mailing; or national advertising.

The applicant contacts his/her school creditor, and/or Sallie Mae to request further information.

Sallie Mae mails an application package including the required certification form to the borrower. The certificates are used to verify that the underlying loans are NDSL, GSL, and/or FISL.

The borrower completes the application and borrower portion of the certificate. The completed forms are returned to Sallie Mae.

The application and certificate are reviewed by Sallie Mae and pay-off date (60 days in the future) is assigned.

Certificates are mailed to the creditors.

The creditors complete and sign the certificates which provide account information, quote and required payoff as of the date projected above, and certify the information. The form is then returned to Sallie Mae.

Sallie Mae prepares a promissory note, which includes the repayment schedule selected by the borrower, and mails the note to the borrower for signature.

The borrower reviews the promissory note, signs it, and returns it to Sallie Mae.

The note is reviewed and payoff checks are mailed to the original creditors.

A coupon book is then sent to the borrower. Repayment begins in 60 days.

(NOTE: Creditors are expected to return obligatory documentation to the borrower based on their standard operating procedures.)

However, because the program (1) requires signed documentation, (2) is supported through the mail, and (3) requires input from both borrower and multiple creditors, it is much more complex than would otherwise be obvious:

When borrowers receive an application, they often do not complete it right away. Borrowers procrastinate because: The application terminology is unfamiliar, they do not want to lose their grace period, they are out of town when the application arrives, they have questions about the product, or it takes time to gather the information necessary for completion.

If a borrower does not complete the application on a timely basis, he/she can miss the opportunity to enter loan repayment under the OPTIONS Program. This causes creditor dissatisfaction because conversion is the most costly phase of student loan processing.

The product concept is simple. The product benefits become complex. Borrowers do not understand: Who qualifies, what the terms of the loan will be, how to choose which Option is right for them, or the intricacies of the decision-making process involved in deciding financial alternatives with which they must live for up to 20 years.

In fact, we find borrowers do not understand many financial details vis-a-vis student loan indebtedness.

They don't know who their creditors are while in grace.

They don't understand reassignment, i.e., the purchase program.

They don't know if thier loans are GSL, NDSL, or FISL.

This results in calls to the consolidation center. Three-fourths of those who consolidate will call the consolidation center with questions sometime during the consolidations process.

Each caller, on average, calls twice.

Each call last five minutes.

In many cases, we are asked to play the role of financial advisor; for example, we are asked to advise about which Option and term the borrower should choose.

Due to the transient nature of the borrower population, certain borrowers do not receive the application after it is mailed. This causes: Phone calls to Sallie Mae to request a new application, and the process of mailing applications must be repeated.

Since the legislation authorizes OPTIONS to payoff only principal and accrued interest, the payoff has to occur on the prescheduled date. This causes the application process to be time sensitive and delays caused by incomplete or incorrect information become problematic.

Critical information, such as creditor name and address, is required to process the application. Lack of information: Necessitates a phone call or letter to the borrower, which usually takes two tries; when reached, the phone call averages ten minutes.

Often there is borrower confusion over the $5,000 and $7,500 debt levels.

We thus get applications from those who don't qualify because of the misunderstanding of single vs. multiple debt, and/or the inclusion of interest.

Those on the border of qualifying in the grace period are forced to wait until repayment to apply (so they will qualify), which causes phone calls or letters to answer questions.

The process is mail oriented. All paperwork must be signed. The characteristics of the population are transient and mail forwarding causes delays which create process hold-ups and redundancies.

Each problem that arises causes a phone call between the borrower and Sallie Mae. This results in the use of a considerable amount of customer service time and causes delays which affect product delivery on the scheduled date. This affects the amount required to pay the underlying debt in full.

Certificates are returned with the borrower portion incomplete. Because OPTIONS is a GSL loan and the OPTIONS documentation supports the validity of the underlying loan, in the event of a future claim the application cannot be processed without a signed certificate.

We must call the borrower or creditor to obtain the information (creditor name, address, and borrower balance).

Each call on average lasts 15 minutes and requires 2 tries.

Creditors often delay returning certificates to Sallie Mae.

We must send a letter to the borrower advising of the delay and the potential effect it will have on the closing schedule.

Delays cause pay-off dates to be missed.

The delay causes additional interest accruals, and makes certificate updates necessary.

Delays require calls to creditors and/or borrowers.

Some creditors have trouble completing the certificate or confuse the program with a loan purchase program.

Creditors confuse grace, deferred, delinquent,and default statuses, and report them in error.

They will call the consolidation center for help.

They will refuse to verify the certificate because it is viewed as competitor request as opposed to a client request.

Letters to follow-up these delays are often met with resistance, creating additional follow-ups and delays.

When borrowers are notified that their creditors have not returned the certificates, and are urged to contact the creditor to remedy the situation, they call Sallie Mae to ask help in getting the institution to cooperate in the consolidation process.

This requires additional phone conversation with the borrower, and requires a call to the bank, school, or guarantor.

When all of the borrowers certificates are returned, the certificates are often returned with different debt levels than the borrower indicated on the application. This may cause: Calls to the borrower or creditor, or a restart of the certificate process.

At times, certificates will indicate the borrower is delinquent or in default. A decline will result and may generate a call from the borrower.

Some statuses are obviously in error and are remedied by contacting the creditor.

Once all of the certificates are reviewed and verified as complete, the promissory note is prepared and sent to the borrower.

Borrowers sometimes hesitate to sign the promissory note when they receive it because:

This is the first time they may have seen the full disclosure of all debt, and they are unsure it is accurate.

They want to select a different repayment schedule.

This causes missed payoffs, requiring certificate updates and generation of new promissory notes.

If the note is not signed and sent back to us within the allowed time, the borrower misses the payoff date. This requires: Certificate updates, communication with the borrower and all creditors, and a new promissory note.

The GSLP is theoretically a national uniform system of loans. In reality it is not. Every guarantor has a slightly different set of rules to be followed in the creation of the documentation of a GSL. Implementation on a state-by-state basis is subject to diverse state statutory and regulatory procedures. This has created substantial servicing problems in the GSLP. Lack of uniformity in the GSLP means that each set of rules requires a different servicing system, and creates uncertainty as to the availability of servicing capacity over the life of a student loan.

The potential for crippling complexity for borrowers, students, lenders, and servicers is inherent in the loan consolidation concept unless a nationally uniform system is mandated. Because loan consolidation offers the student a variety of repayment plans, in length of repayment and amount of payment, the permutations and combinations are limitless. For example, if Sallie Mae offers three OPTIONS to the student with a certain level of indebtedness, one fixed repayment and two different graduated repayments; state A may offer five; lender B, two; etc. None of these may be identical or even similar except in respect to the basics such as interest rate. This will create the necessity for different servicing computer routines for each type of consolidated loan most of which will probably be incompatible. Therefore, an existing system, such as Sallie Mae has, will be unable to service non-conforming loans.

Further, the documentation, the forms, and procedures can vary widely; they do in GSL, and the potential is vastly greater in consolidation. Lenders in confirming loans and providing documentation necessary to determine indebtedness would be faced with multiple sets of guidelines and documents which may tend to inhibit cooperation and support for consolidation. Borrowers may be presented with innumer-

able choices for consolidating their indebtedness, each slightly different, leading to confusion and artifically inhibiting the borrower from taking advantage of consolidation. This confusion may also affect the overall financing plans as early as high school because of the uncertainty of the terms and conditions which will be available to repay student loan debt.

We believe a national uniform system is an absolute necessity in this program. To allow a proliferation of non-conforming paper will overburden an already strained servicing system. Mortgages have moved in precisely the opposite direction, there is now a national system of documentation for home mortgages. Such a concept is possible for student loans and an absolute necessity for loan consolidation. At a minimum, however, we sincerely believe the standards for loan consolidation must be uniform if we are not to create a bewildering array of non-conforming programs which will confuse students, and create havoc for the delivery system.

We have reviewed the testimony of Dr. Edward Elmendorf of May 25, 1983, presenting the views of the Department of Education on student loan consolidation. As you requested, we have set forth below our reaction to those concerns. We believe the technical concerns can be easily resolved and we suggest that the cost to the federal government is a policy determination best left to Congress.

Dr. Elmendorf's testimony discussed several problems with the current law authorizing Sallie Mae's OPTIONS Program. The 7 percent interest rate for the current consolidation program ought to be adjusted. We have testified that the interest rate could match the borrower's GSL interest rate without creating a disincentive to the program and would endorse such a statutory change.

Sallie Mae is not currently consolidating either ALAS or HEAL loans. We do not believe that the concept of weighted average interest rates is a viable one. Under the current Sallie Mae OPTIONS Program, borrowers are provided 48 different payment plans to match the new payments with their particular financial situation. We believe that maximum borrower participation in the financial decision helps reduce the likelihood of default. If weighted rates were applied, the number of permutations and combinations of monthly payments would be infinite, and the borrower could not be informed up front of the new payment schedules until after the new promissory notes were generated. The federal government interest billing currently requires that the bill be itemized by stated interest rate and separated by their origination date (some loans have a different special allowance payment rounding formula depending on the date originated). It would be extremely difficult to accurately generate and control the government interest billing if weighted rates are reported to and must be validated by the Department of Education. The reduction in monthly payments to borrowers would virtually be nil, while the administrative complexities would be substantial.

The Department points out that, as written, the statute applies all the requirements of section 427 of the Act to the loan consolidation program. We believe these requirements should be reviewed and the loan consolidation program be exempted from those which are not viable such as the student endorsement provision. We will be pleased to review these technical points with your staffs.

We agree with the underlying concern of the Department on the establishment of flexible repayment terms; that there be a national uniform system. However, we do not agree that the statute, as written, allows Sallie Mae or would allow any other lender offering consolidation to unilaterally disregard statutory provisions as to the terms of repayment. We would note, however, that as the Department has been the sole guarantor of our consolidation loans, we have been able to agree, as a condition of the guarantee, to appropriate limitations not only in this respect, but in other technical issues such as that discussed in the preceding paragraph.

The Department's concerns about extension of loan consolidation to other lenders are primarily of a policy nature. We would note in this connection that Sallie Mae does not receive administrative cost allowances, it is funded on a fully taxable basis, and pays federal income taxes. As we have stated, Sallie Mae neither requests nor requires a monopoly. We leave this policy determinations to the Congress.

As Dr. Elmendorf noted, there are significant costs to the federal government from existing programs financed through the issuance of tax-exempt securities. The Estimate of Federal Tax Expenditures prepared for the Committee on Ways and Means and the Committee on Finance in March, 1983, by the staff of the Joint Committee on Taxation, states that the exclusion of interest on state and local government student loan bonds will cost the federal government more than $2.6 billion in revenues foregone during Fiscal Years 1983-1988. This is based on continued use of revenue bonds to finance the GSLP and is actually understated relative to the amount of bonds currently outstanding. In addition, the state agencies which are financed through the issuance of revenue bonds, and which earned approximately

$150 million in Fiscal Year 1982, are exempt from federal income tax on these profits. This substantially increases revenue lost to the federal government. In order to offset these losses, in 1980 Congress reduced the special interest allowance by half for those loans prospectively acquired or originated by tax-free entities. However, the experience of the past three years has shown the federal revenue loss potential from state agency tax-exempt revenue bonds was substantially greater than anticipated. Department of Education data indicates that there were less than $1 billion of loans eligible for the half special allowance during the first quarter of Fiscal Year 1983. Assuming that these were all 7 percent loans, the first quarter offset to the federal government in reduced special allowance payments was approximately $6 million. Assuming that these loans were 9 percent, which is more probable, the federal offset was approximately $3.5 million. Based on Congressional Budget Office (CBO) and Office of Management and Budget (OMB) interest rate forecasts for the next five years, the halved special interest allowance savings will remain minimal relative to the billions of dollars of revenue losses to the federal government. Additionally, because the minimum yield on student loans to tax-exempt entities has been set at 9½ percent, while other holders have a minimum yield of 9 percent on the same loan, under the interest rate forecasts there will actually be periods during the next five years when the U.S. Treasury will be providing additional subsidy.

We have had the opportunity to review the testimony of Mr. Morton E. Henig, Senior Associate Director, Human Resources, General Accounting Office, before the Joint Committees on May 25, 1983. Mr. Henig and his associates spent many months evaluating the student loan consolidation program and Sallie Mae's management of the OPTIONS Program. We look forward to receiving the final report of this study from GAO and believe that it will indicate that loan consolidation is a worthy program and that Sallie Mae has administered its responsibility fairly and in a manner that is consistent with its legislative mandate.

It is important to note that in the GAO report various state agencies have indicated the capacity to provide a loan consolidation program and that they have the financial and operational wherewithal to accomplish this task. The GAO did conclude that the state agencies appear to have the financial ability because of their success in marketing low-yielding, tax-exempt student loan revenue bonds. However, it is our understanding that the GAO did not audit or test the assertion that systems and controls are already in place or that consolidation was similar to functions currently being undertaken by the states, thereby reaching a GAO conclusion relative to the operational capacity of the state agencies. The GAO report stated that, "According to officials of the eight state programs, their program functions for servicing, purchasing, and making student loans are similar to those required to consolidate loans. . . ." This statement was reported, rather than confirmed by GAO analysis. Based on our experience, we think it most unlikely that the capacity to operate a consolidation program currently exists. However, we do not believe that performing loan consolidation is beyond the capacity of others to initiate, assuming an appropriate expenditure for staff, systems, and controls.

Mr. Henig's report also makes clear that the GAO was not able to perform an analysis of the costs to the federal government associated with the extension of the program to entities financed by tax-free securities. However, it should be noted that studies by the Treasury Department, the CBO, the Joint Committee on Taxation, and the testimony of Dr. Edward Elmendorf of the Department of Education on May 25, 1983, before this Committee on behalf of the Administration, have concluded that there is a significant loss of revenue to the federal Treasury through the issuance of tax-exempt revenue bonds for this purpose.

We have begun to notify borrowers who have already applied for consolidations scheduled to occur after August 1 of potential problems. We are especially concerned that certain borrowers in repayment whose current level of indebtedness is close to the statutory minimums may lose their entitlement to a consolidation loan if their outstanding balance drops below $5,000 or $7,500 during any temporary moratorium on the program. The following notice is now provided to all applicants:

"IMPORTANT NOTICE

"As with many federal program, Congressional authorization for loan consolidation includes a program termination date. This authorization expires on August 1, 1983.

"Sallie Mae has been advised in connection with recent Congressional hearings on reauthorization, that the Congress will make every effort to extend the program prior to the August 1, 1983, termination date. However, in the event that this exten-

sion is delayed, it will be necessary for Sallie Mae to postpone the final steps in processing your application. In the unlikely event that a change in our authorization that affects your application occurs, we will notify you promptly. We recommend that you submit your application upon receipt with the assumption that a timely reauthorization will be forthcoming.

Thank you for your interest in Sallie Mae—OPTIONS."

We hope you will be able to proceed swiftly with this legislation so that we may continue to offer consolidation.

We are, as always, available to provide any technical assistance you or your staffs require. We hope you will consider the impact of statutory change on the complex process of consolidation as you deliberate. Thank you for this opportunity to express our concerns.

Student Loan Consolidation Center P.O. Box 1600 Merrifield, VA 22116 (800) 446-4000

SallieMae

OPTIONS

Dear Applicant,

Thank you for your interest in OPTIONS. Enclosed are all the materials you will need to apply. The following forms have been included:

One Instruction Sheet
One Application
One Certificate (Two if you listed more than 3 creditors)
One #10 Postage Paid Envelope to return the completed application and certificate to Sallie Mae
One OPTIONS Selector
One Benefits Comparison Chart

If any of the forms are missing, or if you have questions regarding their completion, please call 800-446-4000.

As soon as we receive your completed application and certificate(s), we will begin processing your request. It will take about 60 days. If any delays occur during the processing, you will be notified.

We feel we have a very attractive plan for you and look forward to receiving your application. Why not complete the forms *TODAY!* and let OPTIONS work for you?

Student Loan Consolidation Center

Enclosures

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SallieMae

STUDENT LOAN MARKETING ASSOCIATION
GENERAL INFORMATION ABOUT YOUR APPLICATION

OPTIONS

About The Program

OPTIONS was authorized by Congress for implementation by the Student Loan Marketing Association (Sallie Mae). With the soaring costs attendant to obtaining a post-secondary education, many students find themselves borrowing under either or both the Guaranteed Student Loan Program (GSLP), and the National Direct/Defense Student Loan Program (NDSL). Of course, increased costs mean larger loans and that means higher payments when the loans must be paid back. Because of these higher payments some ex-students have found themselves unable to meet their obligation(s) and they end up failing to repay their debt. OPTIONS is offered as one way to reduce the default rate. By consolidating several loans and/or extending repayment terms, the debt becomes more manageable for the borrowers. The net result will be fewer defaults and overall lower cost for the government (TAXPAYER) to support the program.

The instructions which follow are intended to help you complete your application both quickly and accurately. Please feel free to contact us if any questions arise while you are filling out the forms.

Qualification

- In order to qualify for OPTIONS you must have over $5,000 (principal + interest) outstanding in guaranteed student loan indebtedness made under either the National Direct/Defense Student Loan Program (NDSL), the Guaranteed Student Loan Program (GSL), and/or Federally Insured Student Loan Program (FISL).

- If you owe between $5,000 and $7,500, your indebtedness must be to more than one creditor or under both programs, or if all loans are GSL loans, insured by more than one guarantee agency. The multiple indebtedness criteria are not applicable if you owe more than $7,500 on your qualifying student loans.

- You are not required to consolidate all of your qualified student loans, but all of the loans you want to consolidate must be current. Delinquent, defaulted, or deferred loans do not qualify for consolidation. This includes loans that become delinquent during the consolidation process.

The Process

After you have reviewed the material in the package, your next step is to complete the application and select your OPTION. Then complete the top half of the verification certificate and return both the application and certificate to Sallie Mae in the postage-paid envelope provided for that purpose.

Upon receipt of your signed application, Sallie Mae will: 1) Assign a scheduled payoff date 60 days from the day we receive your package, and 2) forward the certificate(s) to your creditor(s) for completion. When your creditors have returned the certificates we will prepare a Promissory Note and mail the new note to you for your review and signature. The promissory note will:

- Show how much and when Sallie Mae will pay each creditor.
- Disclose the interest rate, total loan amount, total interest to be paid, and the OPTIONS repayment schedule you selected.

When you return your signed Promissory Note to us we will mail the check(s) to your creditor(s) for the amounts stated on the Note. Each check will be payable to your creditor to be applied against your student loan account. We will notify you of the check remittance and explain your repayment obligations.

Within 30 days after you receive this notice you will receive your first bill from Sallie Mae.

We estimate that it will take between 45 and 60 days to complete the process. This timing assumes a quick response from you and your creditor(s). *During this period it is critical that you continue making payments on your existing loan(s)!*

Forms Completion

Before proceeding, please inventory the package and make sure you have all the forms indicated on the cover letter. If you don't — call us at (800) 446-4000.

The application, certificate and OPTIONS SELECTOR have instructions detailing how to complete (or use) them. Some highlights on each form may be useful:

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Application

- Make sure to include your Social Security number and sign and date the form.
- Complete the Student Loan information section as best you can. While the amount owed does not have to be exact, if you know your exact balance(s), it will help speed up the process. If you don't know the answers to these items you may want to call your creditor(s) and verify your record(s). This will also help you complete the Certificate information. Please compare the three Repayment Options available in the OPTIONS SELECTOR, select the one that best fits your needs and then indicate your choice in the OPTIONS Section.
- Mail the form to Sallie Mae in the enclosed postage-paid envelope.

Certificates

- The verification certificate is a multipart form designed so you only need to complete the information one time. This form is used to authorize your creditors to release information about the loan(s) you want included in the consolidation. One certificate will provide information for up to 3 creditors.
- Make sure to provide a complete mailing address for each creditor.
- You must provide the account information requested.
- The form MUST be SIGNED and DATED.
- Enclose the completed certificate(s) in the postage-paid envelope with the application and return them both to Sallie Mae.

OPTIONS Selector

This pamphlet illustrates the three repayment plans available to you. The number of different monthly payments you may choose from is based on your total outstanding balances. This booklet is provided as a guide to aid you in your selection. The amount of monthly payments may differ slightly from that on your Promissory Note. Assuming your estimated balance is correct and agrees with your creditor(s) and you use the selector properly, your OPTIONS Promissory Note and repayment schedule will reflect the plan and monthly payment term you chose.

Your New Loan

When your loans are consolidated the new OPTIONS loan you receive will be from Sallie Mae. The OPTIONS loan will be a GSL bearing a 7% interest rate (Annual Percentage Rate). Your new OPTIONS loan enters repayment status the day it is made and the first payment will be due within 60 days of the date the check(s) are mailed to your creditor(s).

IMPORTANT!!! Every effort will be made to remit the payoff amount to the creditor on the scheduled date. Occasionally, however, the exact amount required to pay the old loan will not be remitted because the payment is not received on the originally scheduled date. In the event of underpayment or overpayment *it is your responsibility* to resolve any difference with your creditor and to take the required action to pay the old loan in full.

Since the new loan is a GSL, the NDSL benefits* you now have will no longer be applicable. The NDSL(s) you consolidated is/are paid in full. (See important note above). However, you will be eligible for the GSL benefits* that exist when you consolidate. Your OPTIONS loan will bear the same basic benefits as other GSL loans and you will have the same basic rights and responsibilities to Sallie Mae as you did to your previous GSL creditors. These will be detailed in the Promissory Note. You should be aware that if you consolidate an NDSL loan, you will lose the lower NDSL interest rate and forgiveness of repayment due to teaching.

**See the enclosed benefits chart for a description of these benefits.*

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OPTIONS

APPLICATION INSTRUCTIONS

IMPORTANT: Detach this sheet, carefully read the instructions that follow, and retain for future reference. Type or print clearly all information requested.

TWO EASY STEPS

Step 1. Complete all items in the Application.

Step 2. Mail the application to Sallie Mae immediately in the enclosed postage-paid envelope.

Item No.	ENTER THE FOLLOWING INFORMATION:
1.	Your name and complete address.
2.	Your social security number must be given. If incomplete, the application will be returned.
3.	Your birthdate.
4.	A telephone number where you can be reached during the day hours.
5.	A telephone number where you can be reached during the evening hours.

STUDENT LOAN INFORMATION

6. The full name of each of your student loan creditors to whom you are sending certificates.

7. Either "GSL" (Guaranteed Student Loan) or "NDSL" (National Direct or Defense Loan) depending on the student loan program under which the corresponding loan was made. Other student loan programs do not qualify for consolidation under the OPTIONS program.

8. The initials of the guarantee agency which insured your GSL student loan. Refer to the guarantee agency codes on the reverse side of the certificate if you do not know these initials. Enter "N/A" if corresponding loan is an NDSL loan.

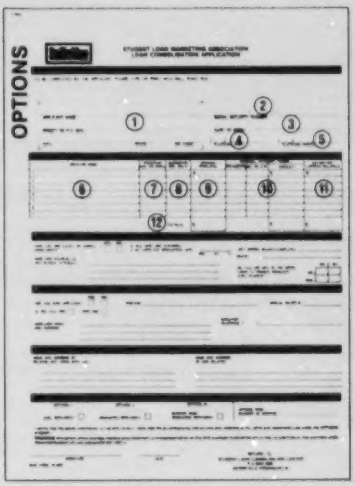
9. The original principal amount of each loan.

10. Original Payment Terms. Enter in the corresponding blocks the repayment terms for each account. This information can be obtained from the Repayment Schedule or Disclosure Statement provided by your creditor.
   - # Payments—the total number of payments.
   - Monthly or Quarterly—how often you make each payment.
   - Payment Amount—amount of each payment.

11. The amount now outstanding with each creditor (principal plus unpaid accrued interest, if any).

12. The sum of each column in the appropriate Total block.

NOTE: Item 11 "Total" must be at least $5,000 to be eligible for consolidation.



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SCHOOL INFORMATION

13. Your graduation/school separation date in the appropriate blocks.

14. The name and address of the last school you attended.

15. The last degree you sought. For example: BA, BS, MBA, MD, JD, etc. Enter one of the following codes for your major course of study:

16.

Code	Classification Code
01	Agriculture/Natural Resources
02	Arts/Communication
03	Architecture
04	Business/Finance/Computer Science
05	Engineering/Technical
06	English/Journalism/Foreign Language
07	Forestry/Environmental Science/Geography/Geology
08	Health/Medicine/Nursing
09	Home Economics
10	Law/Government Service/Political Science
11	Math/Statistics
12	Philosophy/Psychology
13	Religion
14	Scientific/Library Science
15	Social Science/History
16	Teaching
17	Trade/Industrial Training
18	Other

17. This item must be completed.

EMPLOYMENT INFORMATION

18. Appropriate data about your employment status.

19. Your employer's name and address (if applicable).

REFERENCES

20. Enter the full name and complete mailing address of a relative not living with you.

21. Enter the full name and complete mailing address of a non-relative not living with you.

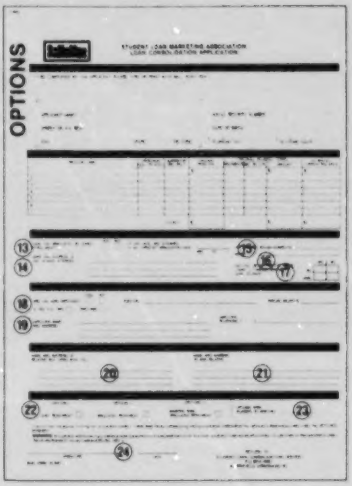
OPTIONS CHOICE

22. Select your desired repayment option and enter an "x" in the corresponding box. Refer to the OPTIONS Selector for instructions and guidance in selecting the right option for your circumstances.

23. Enter the term (number of months) you desire for your OPTIONS repayment period. Refer to the OPTIONS Selector for assistance in making the appropriate choice.

NOTE: If you fail to complete these items, Sallie Mae will give you OPTION I with the shortest term.

24. Sign and date the Application and return both copies to Sallie Mae.



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OPTIONS

SallieMae

STUDENT LOAN MARKETING ASSOCIATION
LOAN CONSOLIDATION APPLICATION

TO BE COMPLETED BY THE APPLICANT. PLEASE TYPE OR PRINT WITH BALL POINT PEN.

APPLICANT NAME _____ SOCIAL SECURITY NUMBER _____

STREET OR P.O. BOX _____ DATE OF BIRTH _____

CITY _____ STATE _____ ZIP CODE _____ ( ) TELEPHONE (DAY) _____ ( ) TELEPHONE (NIGHT) _____

STUDENT LOAN INFORMATION

CREDITOR NAME	PROGRAM (GSL OR NDSL)	LOAN NO. (SEE LABEL)	ORIGINAL PRINCIPAL	ORIGINAL PAYMENT TERMS: PAYMENTS/ME OR QTR	AMOUNT	ESTIMATED CURRENT BALANCE
1			$		$	$
2						
3						
4						
5						
6						
7						
		TOTALS	$		$	$

SCHOOL INFORMATION

HAVE YOU GRADUATED OR LEASED ENROLLMENT? YES ☐ NO ☐ IF YES, DATE LAST ATTENDED _____ IF NO, EXPECTED GRADUATION DATE _____ MM DD YY

LAST DEGREE SOUGHT/COMPLETED _____ MAJOR _____

NAME AND ADDRESS OF LAST SCHOOL ATTENDED _____

DID YOU USE ANY OF THE ABOVE LOANS TO FINANCE GRADUATE LEVEL STUDIES? YES ☐ NO ☐ GSL ☐ ☐ NDSL ☐ ☐

EMPLOYMENT INFORMATION

ARE YOU NOW EMPLOYED? YES ☐ NO ☐ POSITION _____ ANNUAL SALARY $ _____

IF YES, FULL TIME ☐ PART TIME ☐

EMPLOYER NAME AND ADDRESS _____ EMPLOYER TELEPHONE ( ) _____

REFERENCES

NAME AND ADDRESS OF RELATIVE NOT LIVING WITH YOU _____ TELEPHONE ( ) _____

NAME AND ADDRESS OF NON-RELATIVE _____ TELEPHONE ( ) _____

OPTIONS CHOICE

OPTION I LEVEL REPAYMENT ☐ OPTION II GRADUATED REPAYMENT ☐ OPTION III SHORTER TERM GRADUATED REPAYMENT ☐ OPTIONS TERM (NUMBER OF MONTHS) _____

I certify that the above information is true and correct. I have read the accompanying instructions and understand my rights and responsibilities under the OPTIONS program.

WARNING: Any person who knowingly makes a false statement or misrepresentation on this form is subject to penalties which may include fines or imprisonment under the United States Criminal Code and 20 USC 1097.4

_____ SIGNATURE _____ DATE

SLCC FORM 101-697

RETURN BOTH COPIES TO:
STUDENT LOAN CONSOLIDATION CENTER
P.O. BOX 1600
MERRIFIELD, VIRGINIA 22116

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OPTIONS

STUDENT LOAN MARKETING ASSOCIATION
LOAN CONSOLIDATION VERIFICATION CERTIFICATE

Dear Student Loan Creditor:

The borrower identified in this certificate has requested that Sallie Mae consolidate certain of his/her eligible student loans. In order for Sallie Mae to provide that service for your customer, it is necessary for you to complete Part II of the certificate.

In an effort to make it easy for you to help your client, we have included instructions for completion of the form. After the information has been completed, simply have the appropriate official sign the form and mail it to Sallie Mae in the enclosed postage-paid envelope. Sallie Mae will then complete the processing of the applicant's request. Both Sallie Mae and the applicant thank you for your assistance in this matter.

GENERAL INFORMATION

OPTIONS, the Sallie Mae loan Consolidation Program, is designed to assist student borrowers in meeting their repayment obligations on their student loans made under the Guaranteed Student Loan (GSL), National Defense or Direct Student Loans (NDSL) and/or Federal Insured Student Loan (FISL) Programs. Borrowers who owe over $5,000 to more than one creditor or who have loans made under any combination of the programs, or who have loans made under the GSL only but which are insured by more than one guarantee agency, are eligible for consolidation in the OPTIONS program. Also, Borrowers who owe more than $7,500 are eligible without regard to the multiple source requirements.

Under the OPTIONS program, the applicant applies directly to Sallie Mae for the consolidation of his/her qualified student loans. The enclosed certificate must be completed by your institution in order to complete the consolidation process. (Please note: your borrower has signed the form requesting release of the information to Sallie Mae.) When all certificates have been received, a promissory note in the aggregate amount of the qualifying certificates is issued to the borrower.

This certificate is necessary to obtain an accurate record of the applicant's current student loan obligations and to determine the payoff amount for your institution. Please complete all of Part II of this certificate and return to Sallie Mae promptly.

NOTE: The payoff date is a date assigned by Sallie Mae. We advise all borrowers to continue meeting their obligations with their creditor(s) until they are notified that the consolidation processing is completed. However, to assure that your institution is paid in full, calculate your payoff figure assuming that no further payments will be made. If you receive a payment from the applicant after completion of the certificate, post the account in the usual manner. When you receive the OPTIONS check for the payoff amount and it overpays the account, please refund the overpayment amount to the applicant.

CERTIFICATE COMPLETION INSTRUCTIONS

Before completing Part II of this form, please review Part I, the applicant's portion to insure that you have adequate information to complete Part II. Contact the borrower at the phone number listed on the form if you cannot process the form because of insufficient information or if there is a significant discrepancy between your institution's records and those of the applicant. By expediting the completion of this form you can insure the payoff check reaches your institution on or before the scheduled payoff date.

CHECK OR ENTER THE FOLLOWING INFORMATION:

1. Verify the account number and type of loan indicated by checking the appropriate box. Please correct account number(s) and type of loan if necessary.
2. **ACCOUNT NUMBER:** Enter your institution's correct account number if different than listed by the applicant.
3. **GUARANTOR:** For each loan made under the GSL Program, enter the initials of the guarantee agency which insures the loan. Refer to the guarantee agency codes table on the reverse side of the certificate.
4. **SLMA OWNED?:** Check the appropriate box to indicate if the loan is already owned by Sallie Mae.
5. **SUBSIDIZED?:** Check the appropriate box to indicate if the loan has been eligible for federal interest benefits while the applicant was in school, grace and deferment status.
6. **DATE OPENED:** Enter the date the loan was made. (If the loan is now in repayment, enter the date of the conversion.)
7. **ORIGINAL AMT:** Enter the original principal amount of each loan.
8. **INTEREST RATE:** Enter the repayment interest rate for the loan.
9. **STATUS:** Refer to the status code table on the form and enter the appropriate code. A default status must be indicated if the loan is in default regardless of the recent payment history.
10. **LAST PAYMENT MADE:** Enter the date the last payment was made if the applicant is making repayments of principal and interest.
11. **NEXT PAYMENT DUE:** Enter the date the applicant's first/next payment is due.
12. **CURRENT PRINCIPAL:** Enter the amount of outstanding principal as of the payoff date assuming that no payments will be made.
13. **INTEREST DUE:** Calculate and enter the amount of unpaid accrued interest outstanding as of the payoff date also assuming that no payment will be made. (If the loan is based on a discounted method of earnings and a rebate will be due, identify the amount of the rebate in this block.)
14. **UNCOLLECTED LATE CHARGES:** Enter the amount of unpaid late charges if applicable.
15. **TOTAL PAYOFF:** Sum the current principal and interest due amounts and enter that amount. (If a rebate was due from step 13, subtract and enter the difference). This figure is the amount you require for the borrower to pay the loan in full on the scheduled payoff date.
16. **PAYOFF REMITTANCE SHOULD BE MADE PAYABLE TO:** Complete this section only if payments from the applicant are to be made payable to an institution different than provided by the applicant. If the loan is an NDSL please indicate the school which will receive credit for the payment.
17. **PAYMENT REMITTANCE ADDRESS IF DIFFERENT FROM ABOVE:** Complete this section only if payments from the applicant are sent to an address different than provided by the applicant.
18. **CREDITOR CERTIFICATION:** Enter the name, title and telephone number of the official who has completed and verified this information. Sign and date the certificate on the appropriate lines.
19. Promptly mail the certificate to the Student Loan Consolidation Center in the postage-paid envelope.

The applicant and Sallie Mae appreciate your assistance in completing this form.

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OPTIONS

SallieMae

STUDENT LOAN MARKETING ASSOCIATION
LOAN CONSOLIDATION VERIFICATION CERTIFICATE

GENERAL INFORMATION: OPTIONS is a program offered by Sallie Mae under which borrowers may apply for a loan to consolidate outstanding loans made pursuant to Title IV of the Higher Education Act of 1965, as amended. The purpose of this form is to obtain verification of the eligibility for consolidation of the borrower's outstanding student loans. Part I of this form is to be completed by the borrower (Applicant) and Part II by the holder of the borrower's loans (Creditor). Please type or print with ball point pen.

PART I TO BE COMPLETED BY THE APPLICANT

(1) APPLICANT NAME AND ADDRESS	(2) DAYTIME TELEPHONE	(3) EVENING TELEPHONE
LAST NAME FIRST INITIAL	(4) SOCIAL SECURITY NO.	
NUMBER AND STREET		
CITY STATE ZIP		

(5)	(6) ACCOUNT NUMBER	(7) BALANCE(S)	(8) CHECK ONE NDSL	GSL
CREDITOR # 1	1			
NAME	2			
NUMBER AND STREET	3			
CITY STATE ZIP				
CREDITOR # 2	1			
NAME	2			
NUMBER AND STREET	3			
CITY STATE ZIP				
(9) CREDITOR # 3	1			
NAME	2			
NUMBER AND STREET	3			
CITY STATE ZIP				
	(10) TOTAL			

I am applying to Sallie Mae for the consolidation of my student loan(s) listed here. I hereby request and authorize the disclosure to Sallie Mae of any information on my student loan(s) listed here which Sallie Mae needs as part of its OPTIONS Loan Consolidation Program.

(11) _____ APPLICANT'S SIGNATURE (11) _____ DATE

CERTIFICATE INSTRUCTIONS

Please complete all of the above information. Type or print clearly (press hard with ball point pen). Complete the following information:

1. Your full name and complete mailing address.
2. A telephone number where you can be reached during the day hours.
3. A telephone number where you can be reached during the evening hours.
4. Your social security number.
5. The full name and complete mailing address of one creditor you want to include in this consolidation.

   Note: If you are making payments to a servicing agent of the creditor, please enter the servicing agent's name. The address you enter should be the same address where you now send payments.
6. The account number assigned to your loan(s) by your creditor. This number will assist your creditor to locate your loan records and process the certificate. If you do not know your account number, enter "unknown".

   Note: Although each loan should be listed separately, you need not repeat the account number if it is the same for all of your loans with the creditor.
7. The balance now outstanding on the loan. If you have more than one loan and your creditor has consolidated the individual loan balances into one repayment schedule, you may enter the aggregate amount outstanding.
8. Check "NDSL", "GSL" (FISL is a type of GSL) depending on the type of student loan program under which the corresponding loan was made.
9. Repeat steps 5-8 for each of your creditors.
10. Sum the individual balances and enter the total amount in the total box.
11. Sign and date certificate.

Review the certificate and make sure that all of the above items have been completed and are accurate. Contact the Consolidation Center if you need assistance in completing this form. Return all parts of this form and the application to the Consolidation Center in the enclosed envelope.

RETURN TO:
STUDENT LOAN CONSOLIDATION CENTER
P.O. BOX [illegible]
MERRIFIELD, VIRGINIA 22116
[illegible]

BEST COPY

OPTIONS

Sallie Mae

STUDENT LOAN MARKETING ASSOCIATION
LOAN CONSOLIDATION VERIFICATION CERTIFICATE

GENERAL INFORMATION: OPTIONS is a program offered by Sallie Mae under which borrowers may apply for a loan to consolidate outstanding loans made pursuant to Title IV of the Higher Education Act of 1965, as amended. The purpose of this form is to obtain verification of the eligibility for consolidation of the borrower's outstanding student loans. Part I of this form is to be completed by the borrower ("Applicant") and Part II by the holder of the borrower's loans ("Creditor"). Please type or print with ball point pen.

APPLICANT NAME AND ADDRESS	DAYTIME TELEPHONE	EVENING TELEPHONE
LAST NAME FIRST INITIAL		
NUMBER AND STREET	SOCIAL SECURITY NO.	
CITY STATE ZIP		

CREDITOR # 1	ACCOUNT NUMBER	BALANCE(S)	CHECK ONE: NDSL	GSL
NAME	1			
NUMBER AND STREET	2			
CITY STATE ZIP	3			

CREDITOR: PLEASE VERIFY ACCOUNT NUMBER(S) AND TYPE OF LOAN

☐ INFORMATION OK AS IS

☐ CHANGES

I am applying to Sallie Mae for the consolidation of my student loan(s) listed here. I hereby request and authorize the disclosure to Sallie Mae of any information on my student loan(s) listed here which Sallie Mae needs as part of its OPTIONS Loan Consolidation Program.

APPLICANT'S SIGNATURE _____ DATE _____

PART II TO BE COMPLETED BY THE CREDITOR

CREDITOR PLEASE NOTE: Total pay-off is the amount you would require the borrower to remit to pay his/her loan in full as of the date to the left.

PAYOFF DATE _____

	ACCOUNT # 1	ACCOUNT # 2	ACCOUNT # 3	ACCOUNT # 4	ACCOUNT # 5
ACCOUNT NUMBER					
STATUS					
GUARANTOR					
SLMA OWNED?	☐ YES ☐ NO	☐ YES ☐ NO	☐ YES ☐ NO	☐ YES ☐ NO	☐ YES ☐ NO
SUBSIDIZED?	☐ YES ☐ NO	☐ YES ☐ NO	☐ YES ☐ NO	☐ YES ☐ NO	☐ YES ☐ NO
DATE OPENED					
ORIGINAL AMT.					
INTEREST RATE					
PAYMENT AMT. INCL. QTR.					
LAST PAYMENT MADE					
NEXT PAYMENT DUE					
CURRENT PRINCIPAL					
INTEREST DUE					
UNCOLLECTED LATE CHARGES					
TOTAL PAYOFF	$	$	$	$	$

STATUS CODES

01 IN SCHOOL	04 DEFERMENT
02 GRACE	05 FORBEARANCE
03 CURRENT REPAYMENT	06 DELINQUENT 30-120 DAYS
	07 DEFAULT

PAYOFF REMITTANCE SHOULD BE MADE PAYABLE TO:

PAYMENT REMITTANCE ADDRESS (IF DIFFERENT FROM ABOVE)

STREET

CITY STATE ZIP

Creditor Certification: To the best of my knowledge the information in Part II is accurate and complete, each loan listed above is a legal, valid, binding obligation of the applicant borrower duly made in accordance with the rules governing either the Guaranteed Student Loan (GSL) Program or the National Direct or Defense Student Loan (NDSL) Program (authorized by Title IV of the Higher Education Act, as amended (20 USC 1070 et. seq.)), each such loan currently is and has been serviced in compliance with all rules applicable to the GSL or NDSL Program as the case may be, and, with respect to a GSL loan, the insurance on such is in full force and effect.

AUTHORIZED OFFICIAL'S NAME _____ SIGNATURE _____

TITLE _____ DATE _____

TELEPHONE _____

RETURN TO:
STUDENT LOAN CONSOLIDATION CENTER
P.O. BOX 1600
MERRIFIELD, VIRGINIA 22116
(703) 385-3600

WARNING: ANY PERSON WHO KNOWINGLY MAKES A FALSE STATEMENT OR MISREPRESENTATION ON THIS FORM IS SUBJECT TO PENALTY OF LAW.

BEST COPY

OPTIONS

SallieMae

PROJECTED DISBURSEMENT DATE _____

Student Loan Marketing Association

PROMISSORY NOTE/PROMISE TO PAY

I, _____ (NAME OF BORROWER), the borrower, promise to pay to the Student Loan Marketing Association, the lender (at P.O. Box 1800, Merrifield, Virginia 22116, or at such other address as designated by the lender), all of the principal sum of _____ $ _____ to the extent it is advanced to me, plus an amount equivalent to daily simple interest on the unpaid principal balance at the rate of _____ percent per year. I will repay this loan in periodic installments in accordance with the Repayment Schedule set forth below. If I fail to pay any of these amounts when they are due, I will also pay all charges and other costs--including reasonable attorney's fees--that are permitted by Federal law and regulations and are necessary for the collection of these amounts. If this loan is referred for collection to an agency that is subject to the Fair Debt Collection Practices Act, I will pay those collection costs which do not exceed 25 percent of the unpaid principal and accrued interest.

ITEMIZATION OF AMOUNT FINANCED

The proceeds of this loan will be used to pay off my liability on the following loans:

	Creditor Name	Amount Paid To My Account With Student Loan Marketing Association	Amount Paid to Other Creditors
1.			
2.			
3.			
4.			
5.			
	AMOUNT FINANCED TOTALS	A. TOTAL	B. TOTAL
		TOTAL AMOUNT FINANCED (A&B)	

The amount paid to each creditor represents the unpaid balance disclosed by the creditor. I understand that if, after payment of the amount listed, there is remaining unpaid balance or an account credit, it is my responsibility to resolve the matter with the applicable creditor.

REPAYMENT SCHEDULE/DISCLOSURE STATEMENT

ANNUAL PERCENTAGE RATE	FINANCE CHARGE	Amount Financed	Total of payments
The cost of the credit as a yearly rate: _____ %	The dollar amount the credit will cost $ _____	The amount of the credit provided to me or on my behalf $ _____	The amount that will be paid after all payments have been made as scheduled $ _____

Repayment of the loan will be in _____ monthly installments, on the same day of each month, according to the following schedule:

_____ payments of $ _____ beginning _____; _____ payments of $ _____ beginning _____

_____ payments of $ _____ beginning _____; _____ payments of $ _____ beginning _____

_____ payments of $ _____ beginning _____; _____ payments of $ _____ beginning _____

_____ payments of $ _____ beginning _____; _____ payments of $ _____ beginning _____

_____ payments of $ _____ beginning _____; _____ payments of $ _____ beginning _____

and a final payment of $ _____ due _____

Late Charge: If a payment is late, I will be charged $5 or 5% of the payment, whichever is less.
Prepayment: If I pay off early, I will not have to pay a penalty.
See the full promissory note for additional terms about nonpayment, default, prepayment, and prepayment refunds and penalties.

If disbursement of this loan is not made on the projected disbursement date, or if a payment is not made as scheduled (e.g., if I make a late payment or if I am entitled to a DEFERMENT), the lender may adjust the repayment schedule.

The lender has provided me with a copy of this Promissory Note, the receipt of which I hereby acknowledge. The terms set forth on the reverse side of this page are part of this Promissory Note. The terms of this Promissory Note will be interpreted according to the law (20 U.S.C. 1071 to 1087-2) and Federal regulations (34 CFR Part 682) that govern the Federal Insured Student Loan Program. I will promptly notify the holder of this loan, in writing, of any change of my name or address.

_____ (SIGNATURE OF BORROWER)

_____ (STREET ADDRESS)

_____ (DATE)

_____ CITY STATE ZIP CODE

SLCC Form 301 9/82

Return To: Student Loan Consolidation Center, P.O. Box 1600, Merrifield, VA 22116

SALLIE MAE COPY

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The lender and I understand that the following terms apply to this loan:

FEDERAL INSURED STUDENT LOAN PROGRAM

This Promissory Note is evidence of a Federal Insured Student Loan which is made pursuant to the loan consolidation authority in Section 439(o) of the Higher Education Act of 1965, as amended (20 USC 1087–2(o)).

PREPAYMENT

I may, at my option and without penalty, prepay all or any part of the principal or accrued interest of this loan at any time.

DEFERMENT

To the extent authorized by Federal law, payments of principal will be deferred after the repayment period begins, provided I comply with the procedural requirements set forth in the Federal regulations governing the Federal Insured Student Loan Program (FISLP), in the following circumstances:

1. While I am enrolled in—
   A. Full-time study at a school that is participating in the FISLP or a school that is an institution of higher education or a vocational school and is operated by an agency of the Federal Government;
   B. A graduate fellowship program approved by the Secretary of Education ("the Secretary"); or
   C. A rehabilitation training program for disabled individuals approved by the Secretary.
2. For a period not exceeding three years for each of the following while I am—
   A. On active duty in the Armed Forces of the United States or serving as an officer in the Commissioned Corps of the Public Health Service;
   B. Serving as a Peace Corps volunteer;
   C. Serving as a full-time volunteer under Title I of the Domestic Volunteer Service Act of 1973 (ACTION programs);
   D. In full-time volunteer service for an organization exempt from income taxation under Section 501(c)(3) of the Internal Revenue Code of 1954, which the Secretary has determined is comparable to the service referred to in clauses B and C above, or;
   E. Temporarily totally disabled, or unable to secure employment because I am providing care required by a spouse who is so disabled (disability must be established by a physician's affidavit).
3. For a period not exceeding two years while I am serving in an internship which the Secretary has determined is necessary for me to gain professional recognition required to begin professional practice or service.
4. For a single period ...* exceeding one year while I am conscientiously seeking but unable to find full-time employment in the United States.

To be granted a deferment, I must provide the lender with written evidence of my eligibility. I must subsequently notify the lender as soon as the condition for which the deferment was granted no longer exists.

INTEREST

1. I will be responsible for payment of all the interest that accrues on this loan.
2. The lender may add any interest that is not paid when it is due, and interest payable by me that accrues during authorized deferment periods, to the unpaid principal balance of this loan, in accordance with Federal regulations governing the FISLP.

LATE CHARGES

If permitted by State law, the lender may collect from me a late charge if I fail to make any part of an installment payment within 10 days after it is due, unless I provide documentation that I am entitled to have the payment deferred as described in this Promissory Note. A late charge may not exceed $5 or 5 percent of an installment, whichever amount is less.

DEFAULT

If I default on this loan, the lender may declare the entire unpaid amount of the loan, including interest, immediately due and payable. A default may also make me ineligible for the benefits described under the DEFERMENT section in this Promissory Note. Under the Federal regulations governing the FISLP, any of the following events could be considered a default: my failure to make a payment when it is due or, in certain circumstances, my failure to notify the lender of a change in my name, address, or school enrollment status.

DISABILITY OR DEATH

If I become totally and permanently disabled, or if I die, my obligation to pay any amount owed on this loan will be cancelled.

CREDIT BUREAU NOTIFICATION

If I default on this loan, the Secretary, using the following procedure, may disclose information about the loan to credit bureau organizations after the Secretary has attempted to collect the debt from me. If the Secretary knows my address, the Secretary must first notify me that such disclosure will be made unless I begin or resume payment. If I do not begin or resume repayment within 30 days of receipt of this notice, or such longer period as the Secretary may specify, the Secretary will disclose information about the loan to credit bureau organizations. If the Secretary does not know my address, the Secretary may disclose information about the loan to credit bureau organizations in order to learn my address. The lender must provide information on the repayment status of the loan to credit bureau organizations upon my request.

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Sallie Mae

YOUR BENEFITS COMPARISON

The chart below compares the major benefits you may now have with the benefits you will have when you consolidate your repayment loans under Sallie Mae's OPTIONS program.

OPTIONS

BENEFIT	NDSL	GSL	OPTIONS
Prepayment allowed	YES	YES	YES
Maximum repayment term	10 Years	10 years	20 years ❶
Interest rate	3%, 4% or 5%	7% or 9%	7% or 9% ❷
Cancellation upon borrower death or total disability	YES	YES	YES
Deferment of principal payments for periods when the borrower is:			
• In attendance full-time at an approved educational institution ❸	YES	YES	YES
• Serving in the Armed Forces, Public Health Service, Peace Corps, VISTA or as a full-time volunteer for certain tax-exempt organizations	YES up to 3 years	YES up to 3 years	YES up to 3 years
• Serving an internship which is required to receive professional recognition and begin professional practice	YES up to 2 years	YES up to 2 years	YES up to 2 years
• Temporarily totally disabled or unable to secure employment by reason of the care required by a spouse who is so disabled	YES up to 3 years	YES up to 3 years	YES up to 2 years
• Seeking but unable to obtain employment	NO	YES up to 12 mos.	YES up to 12 mos.
Six month grace period after deferment	YES	YES ❹	NO
Responsibility for interest during deferment periods listed above and applicable grace periods	No interest accrues during these periods.	Borrower pays, unless the interest on the loan was paid by the Government while the borrower was attending school. ❺	Borrower pays ❺
Partial or full cancellation, over time, of loan for Public Service as:			
• A full-time teacher in certain public or other nonprofit private elementary or secondary schools	YES	NO	NO
• A full-time staff member in certain preschool programs	YES	NO	NO
• A full-time teacher of handicapped children in a public or other nonprofit private elementary or secondary school	YES	NO	NO
• A member of the Armed Forces of the United States for services in an area that qualifies as an area of hostilities	YES	NO	NO

❶ Actual maximum term is based upon total loan balance.
❷ If interest rate on GSL loans being consolidated is 7%, the OPTIONS loan will be at 7%.
❸ Attendance may be on a half time basis but must be at an institution of higher education.
❹ But only for loans made before October 1, 1981.
❺ But required interest payments may be deferred and added to the principal amount of the loan.

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Sallie Mae
has already helped thousands of student loan borrowers cut their monthly payments by as much as half.

Now let us help you.

BEST COPY

Introducing the Student Loan Marketing Association (Sallie Mae) OPTIONS Program

Remember how happy you felt when your student loans came through and eased the worry about how to pay for school? Now that you've graduated you may have a new concern—how to repay your student loans.

Repaying student loans doesn't have to be overwhelming, though. With planning and budgeting, your payments can be manageable. And the Sallie Mae OPTIONS program can help make your loan repayment even more affordable.

How Sallie Mae helps

In 1972, Congress chartered Sallie Mae to work closely with lenders to promote the accessibility of student loan credit. In 1981, we were authorized by Federal law to create a program that would make repayment easier for student loan borrowers. This new service, called OPTIONS, is another way Sallie Mae contributes to the national student loan program. Under OPTIONS your existing student loans are combined into one new, manageable, easy-to-pay loan made under the Federally regulated Guaranteed Student Loan Program. When you take advantage of OPTIONS, you help other students who need loans because the OPTIONS program circulates money back to lending institutions and schools to help them make new student loans.

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How you benefit

You keep more money each month.

Borrowers who have taken advantage of the OPTIONS program have reduced their monthly loan payments by as much as 40 to 50%. This chart illustrates the average reduction for borrowers who have already benefitted from the OPTIONS program.

Loan Category	Average Old Payment	Average OPTIONS Payment	Average Monthly Reduction
$5,001-$7,500	$ 96.00	$ 58.00	$ 38.00
$7,501-$11,000	122.00	72.00	50.00
$11,001-$15,999	166.00	96.00	70.00
$16,000 or more	214.00	123.00	91.00

These savings mean increased financial flexibility for you and more money to spend on the things you need now.

You pick the terms of your repayment.

There are three different OPTIONS repayment plans to choose from. With each plan you write one check, once a month to Sallie Mae. In the next few pages, we'll explain each plan.

How you become eligible

To find out if you're eligible, first add up the approximate amount of money you still owe on your GSL, NDSL, or FISL* loans which are in good standing and which you want to combine. Keep in mind that you don't have to combine every loan you hold. Just as long as the amount adds up to more than $7,500, you are eligible for OPTIONS.

If the amount adds up to more than $5,000, but less than $7,500, you are eligible, but only if your loans are from more than one lender, program, or guarantor.

*Only Guaranteed Student Loans (GSL), National Direct (Defense) Student Loans (NDSL), and Federally Insured Student Loans (FISL) qualify.

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How the program works

Sallie Mae pays off your existing student loans and creates one new loan. If you choose, you can have more time to repay this loan than you had with your original loans. These additional months to repay mean lower monthly payments.

There are three OPTIONS repayment plans to choose from. Your choice should be based on how much you can budget each month for your loan payment, how long you want to take to repay your loan, and your income expectations for the future.

OPTION 1: With OPTION 1, your monthly payment amount will be the same for the entire term of the loan. This amount can be considerably less than the total amount you are currently paying. And you select the payment that best fits your budget. You'll never pay any more than the amount you select. So as your income rises, it's good to know that your monthly payments won't.

OPTION 2: With OPTION 2, your payments start out low and increase gradually. So if you've just become established in your career, this may be the plan for you. It makes your payments manageable now and still affordable later. And, within certain limits, you select how long you want to take to repay your loan. As a result, you can control your cash flow.

OPTION 3: With OPTION 3, your monthly payments start out low, then increase more rapidly than with OPTION 2. So if you expect your earning power to rise quickly, you can pay off your loan with fewer payments. And like OPTIONS 1 and 2, you can choose, within certain limits, how long you want to take to repay your OPTIONS loan.

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How to choose your OPTIONS

The chart below helps you approximate your monthly payment under each OPTION. These are the lowest possible payments for each loan amount and they are based on the maximum number of months you can take to repay your loan.

To see how the OPTIONS program works, find the amount closest to what you currently owe. The maximum amount of time you can take to repay the loan is listed next to each OPTION. For OPTION 1, the approximate monthly payment throughout the life of the loan is listed. For OPTIONS 2 and 3, where payments increase every two years until the loan is repaid, the approximate first, midpoint, and final payments are listed. Remember, you can choose the OPTION you prefer, and, within certain limits, the amount of time to repay the loan.

Total Loan Amount		Maximum Term (in months)	First Payment	Midpoint Payment	Final Payment
$5,000	OPTION 1 (Level)	120	$58	$58	$58
	OPTION 2 (Graduated)	120	39	59	90
	OPTION 3 (Accelerated)	96	39	80	116
$10,000	OPTION 1 (Level)	156	$98	$ 98	$ 98
	OPTION 2 (Graduated)	156	70	105	156
	OPTION 3 (Accelerated)	127	70	109	214
$15,000	OPTION 1 (Level)	192	$130	$130	$130
	OPTION 2 (Graduated)	192	98	130	189
	OPTION 3 (Accelerated)	161	98	152	236
$20,000	OPTION 1 (Level)	240	$155	$155	$155
	OPTION 2 (Graduated)	240	125	160	216
	OPTION 3 (Accelerated)	207	125	179	256

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How to know OPTIONS is right for you

- OPTIONS loans are GSL loans and carry a fixed interest rate of 7%. If you hold any loans with a lower interest rate, you will still save money on your monthly payments with OPTIONS. The money you save now can offset the increased interest rate.
- With OPTIONS, you don't have to worry about any origination fee or any other kind of supplementary charge.
- Only GSL, NDSL, and FISL are eligible for the OPTIONS program. Regular consumer loans or other student loans are not eligible.
- You and your spouse cannot combine your loans, nor can you combine your loans with loans your parents hold.
- As with other GSL loans, you're entitled to deferment rights with OPTIONS. The only difference is the way the interest is handled. With OPTIONS, the government does not pay the interest during deferment. However, interest may be deferred by you and added to the principal amount of the loan.

How to apply for OPTIONS

Now that you know how to lower your monthly student loan payments, simply fill out the attached envelope. We'll begin processing your application for OPTIONS right away. If you still have any unanswered questions, call our Customer Service Center at 800-446-4000 toll free.

BEST COPY

Yes, I'd like to apply for OPTIONS

Name _____

Address _____

City _____

State _____ Zip _____

Social Security Number _____

Daytime Telephone _____

Evening Telephone _____

Date You Last Attended School (Month/Year) _____

How Did You Find Out About OPTIONS?

- ☐ School
  Which one? _____
- ☐ Bank or other financial institution
  Which one? _____
- ☐ Sallie Mae offer
- ☐ Guarantee agency
- ☐ Servicer
- ☐ Newspaper
- ☐ Other media
- ☐ Friend/relative
- ☐ Other

To avoid processing delays, mail this application as soon as possible.

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30-692 O—84—5

Loan Information

LENDER	PROGRAM (NDSL, GSL, OR FISL)	AMOUNT NOW OWED	DATE REPAYMENT BEGAN/WILL BEGIN

TOTAL NUMBER OF:

LOANS_____

LENDERS_____

TOTAL OWED_____

MOISTEN HERE

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OPTIONS SELECTOR

66

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THE OPTIONS SELECTOR

1. Select the amount nearest what you currently owe from those listed at the top of the table.

2. Scan the appropriate column for the monthly payment you'd be most comfortable with.*(For the graduated payment plans—**OPTIONS 2** and **3**—the first figure shows your first 24 payments. The second figure shows your final and highest payments. The % column shows how much your payments increase every two years.)

3. Look to the left of the table to determine the term of your new loan.

If the exact amount of your outstanding loan is not shown, it's still easy to calculate your payments. Say you owe $16,752. Subtract the monthly payment for $16,000 from the monthly payment for $17,000. Multiply the difference by .752, and then add that amount to the monthly payment for $16,000.

If you owe more than $31,000, you can use the additive feature of the selector to estimate your payment amount. For example, the monthly payment for a loan of $33,000 for 20 years is $208 ($100 for $16,000 at 20 yrs + $108 for $17,000 at 20 yrs). **Note: Be sure to use the same OPTION and term length for both parts of your loan.**

In order to use the percent figure under OPTION 2 and OPTION 3:

1. Multiply your selected payment by that percent.

2. Add the product to the beginning payment (this represents payments 25-48).

3. To complete your personalized schedule, continue computing each 2-year increment as above utilizing your last answer as the new starting point.

4. Check your work by comparing your final answer to the final payment listed on the selector.

*The payments are approximations based on an annual percentage rate of 7%. Your actual payment may differ slightly based on your balance and the OPTION you select.

Student Loan Consolidation Center
P.O Box 1600
Merrifield, VA 22116

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	$5,000			$6,000		
[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
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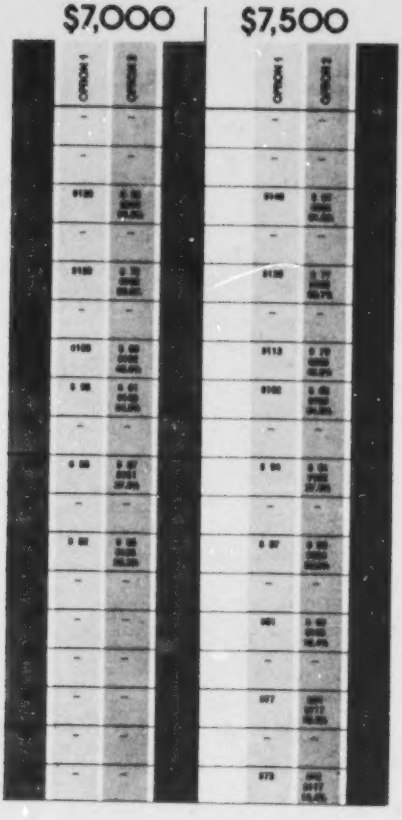

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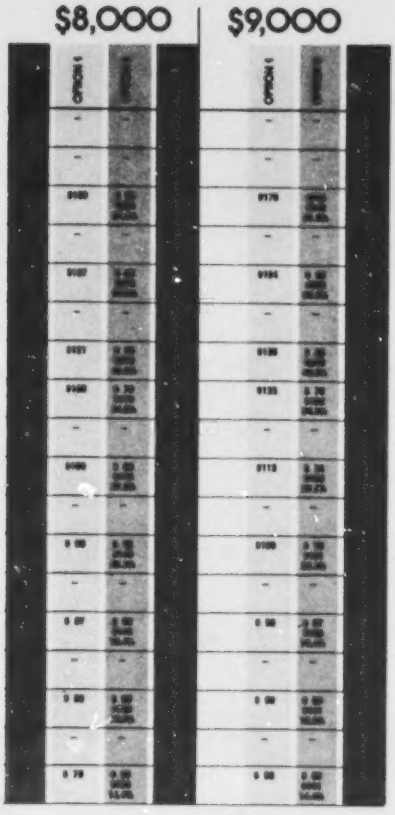

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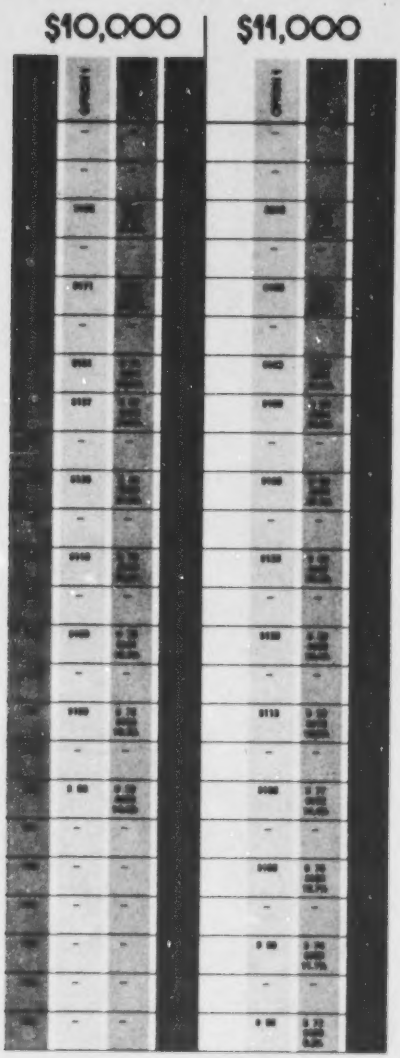

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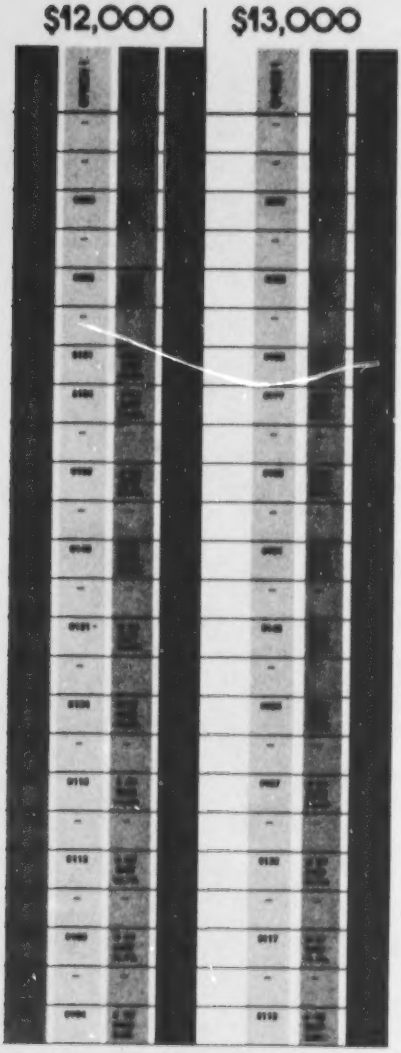

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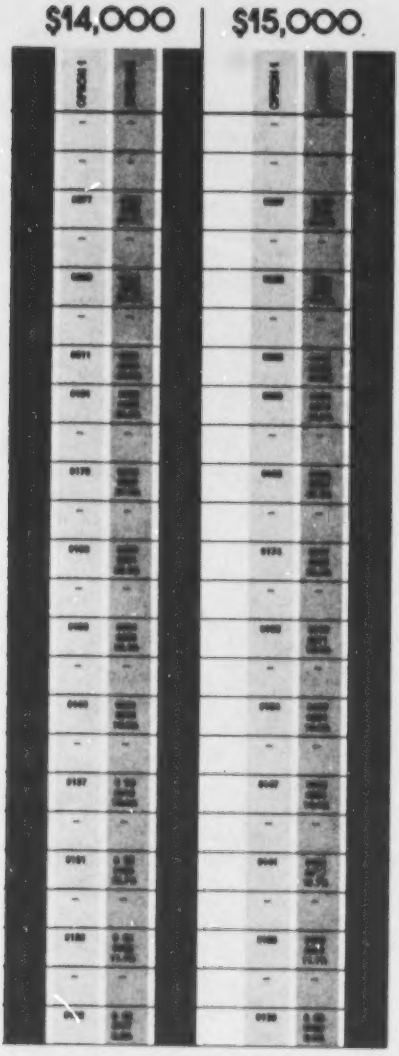

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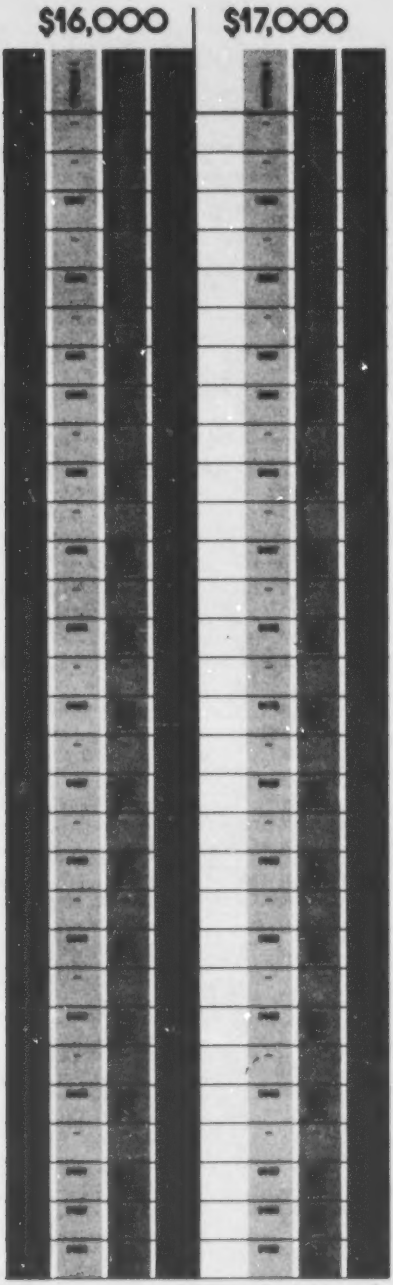

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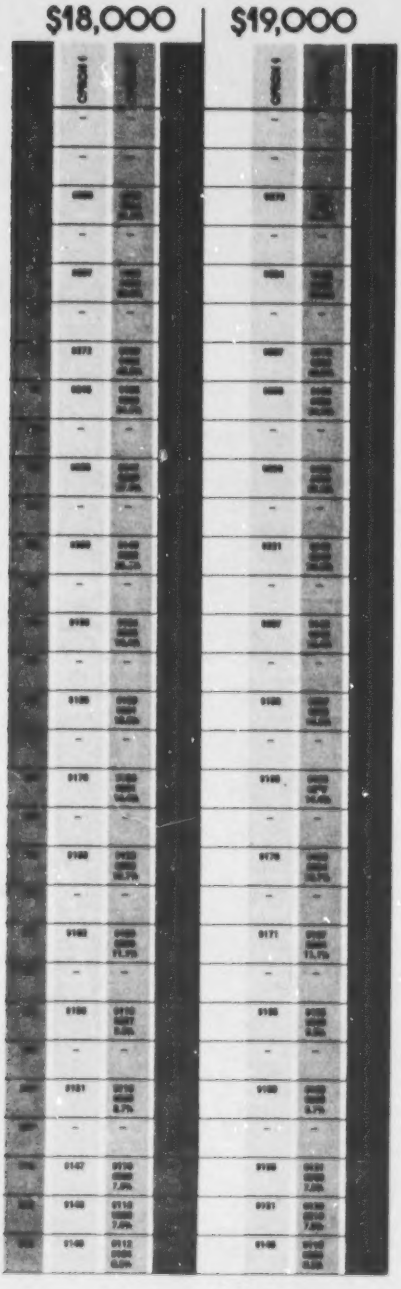

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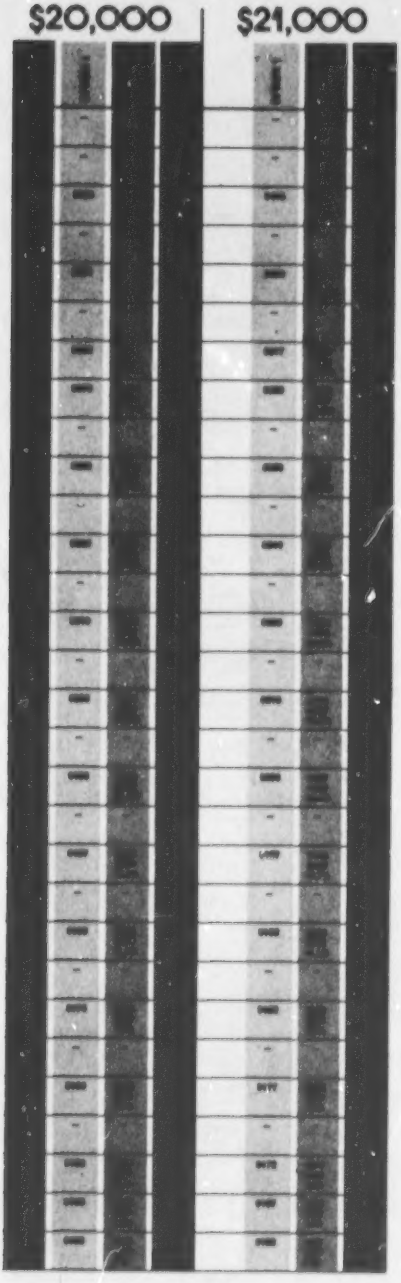

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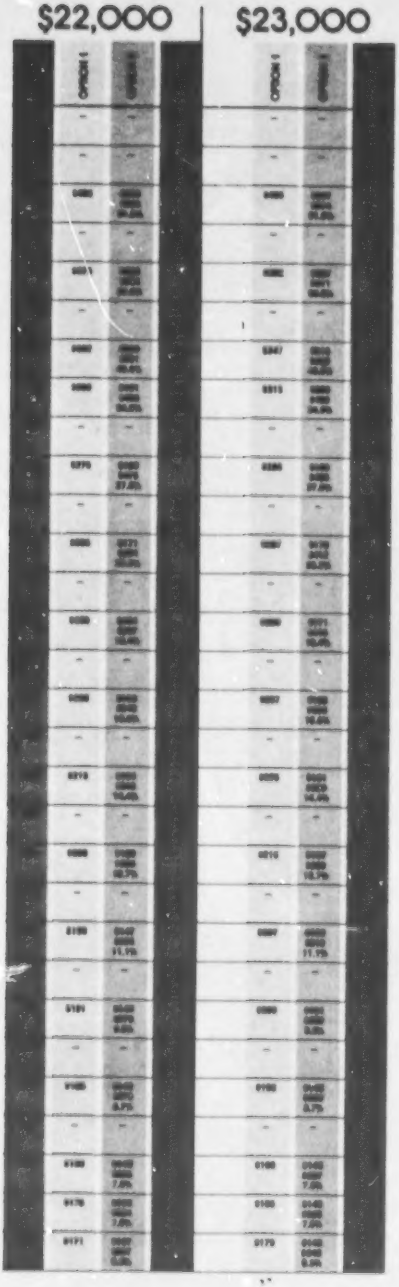

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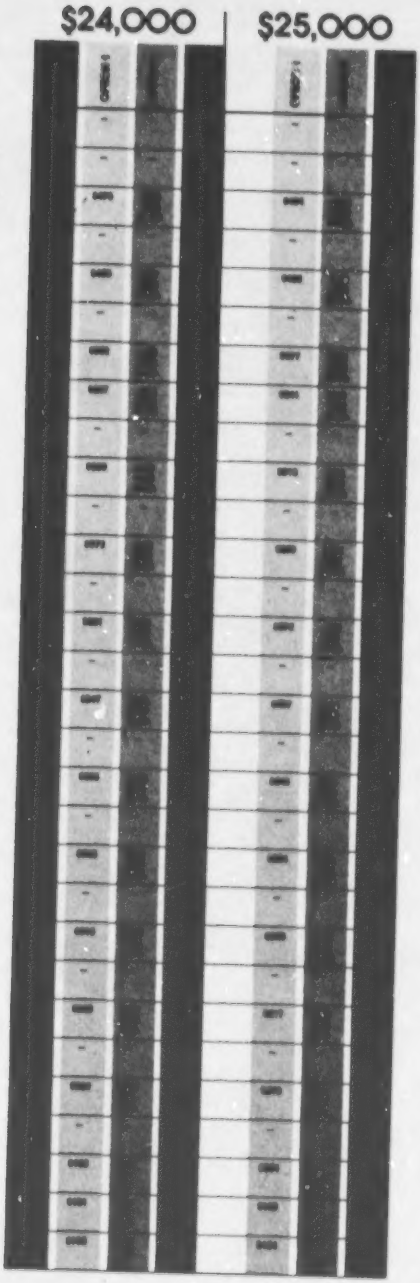

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$26,000				$27,000		
SCCA TIME SPEED	OPTION 1	OPTION 2	OPTION 3	OPTION 1	OPTION 2	OPTION 3
46	-	-	$ 392 $1074 100.0%		-	$ 213 $1110 100.0%
84	-	-	$ 367 $1022 100.0%		-	$ 278 $1080 100.0%
89	9814	$382 9876 61.0%	-	9594	$ 213 $1009 61.9%	-
94	-	-	$ 243 $ 666 58.5%		-	$ 333 $1094 58.9%
72	5443	$287 9891 60.9%	-	9460	$ 275 $ 717 60.8%	-
75	-	-	$ 226 $1138 71.6%		-	$ 324 $1182 71.6%
84	5392	$243 9710 43.0%	$ 212 $ 604 56.0%	9497	$ 253 $ 709 43.0%	$ 226 $ 656 56.9%
96	5364	$226 9663 34.9%	$ 202 $ 566 43.9%	9368	$ 234 $ 674 34.9%	$ 210 $ 633 43.9%
106	-	-	$ 184 $ 547 39.5%		-	$ 261 $ 672 39.9%
108	5325	$212 9561 27.4%	-	9327	$ 220 $ 583 31.0%	-
117	-	-	$ 187 $ 529 29.5%		-	$ 184 $ 560 29.9%
120	5302	$202 9405 23.3%	-	9313	$ 210 $ 553 23.3%	-
127	-	-	$ 181 $ 508 25.1%		-	$ 189 $ 575 26.1%
132	5293	$184 9469 19.4%	-	9294	$ 201 $ 497 19.4%	-
139	-	-	$ 177 $ 466 21.9%		-	$ 184 $ 570 21.9%
144	5261	$187 9405 16.8%	-	9218	$ 194 $ 421 16.8%	-
150	-	-	$ 173 $ 499 18.1%		-	$ 189 $ 487 18.1%
156	5254	$191 9496 14.4%	-	9294	$ 188 $ 421 14.4%	-
161	-	-	$ 170 $ 489 19.7%		-	$ 177 $ 550 19.7%
168	5263	$177 9361 12.7%	-	9253	$ 184 $ 375 12.7%	-
172	-	-	$ 166 $ 419 13.9%		-	$ 126 $ 431 13.9%
180	5234	$173 9361 11.1%	-	9243	$ 188 $ 375 11.1%	-
183	-	-	$ 166 $ 370 12.2%		-	$ 172 $ 394 12.2%
192	5218	$170 9328 9.8%	-	9234	$ 177 $ 341 9.8%	-
198	-	-	$ 164 $ 369 10.7%		-	$ 170 $ 382 10.7%
204	5218	$168 9377 8.7%	-	9227	$ 174 $ 329 8.7%	-
207	-	-	$ 162 $ 332 8.6%		-	$ 168 $ 340 8.6%
216	5212	$165 9302 7.8%	-	9220	$ 172 $ 313 7.8%	-
226	5207	$164 9305 7.9%	-	9215	$ 170 $ 311 7.9%	-
249	5202	$162 9298 6.3%	-	9218	$ 168 $ 301 6.3%	-

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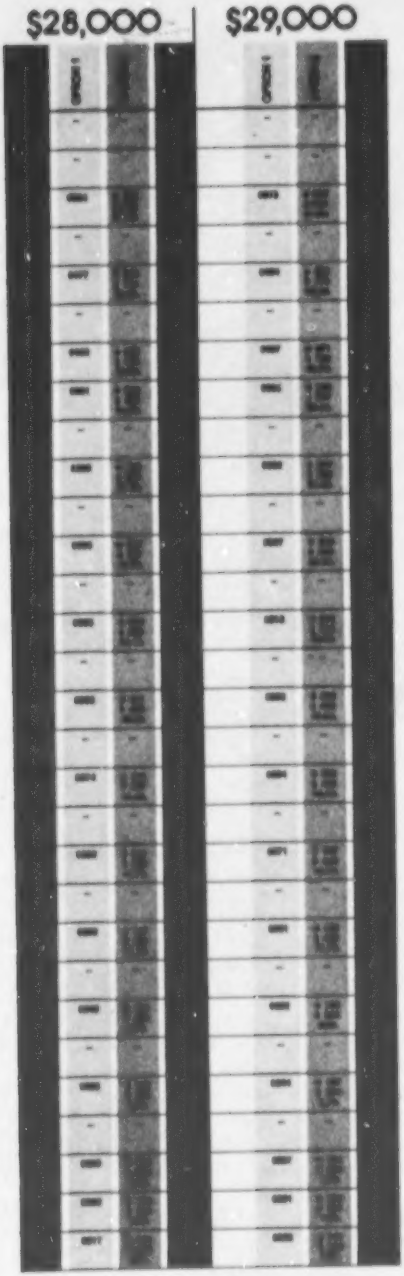

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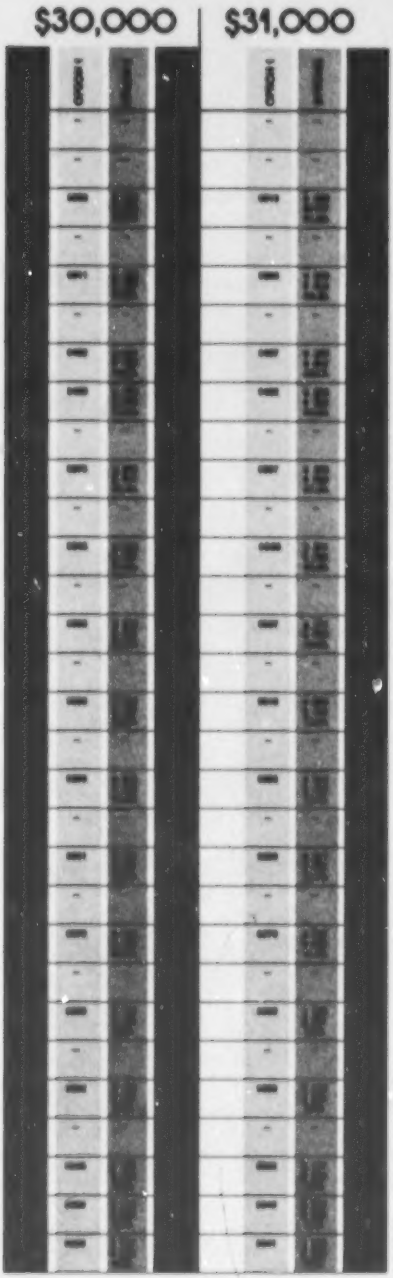

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Mr. Fox. We believe that our program has been workable and has been successful and following a very substantial investment in this program, we think it's doing what the legislation intended for it to do. We would leave to you any policy determinations as to how many programs of consolidation you think should be out there and we would hope also that the issues of complexity, consistency and the like be dealt with in any changes that you might make.

One comment that you made, sir, about defaults, I would challenge. We have had a default rate in the consolidation program of something less than 1 percent, after about 18 months of operation of the program, and while we don't believe that the default rate is going to stay that low, we do know that most of the categories of students, regardless of the amount of indebtedness that they incur have default rates that are substantially higher than that.

There is no really good evidence as to what default rates are, there are definitional changes constantly in this thing, but we do that a significant number of students will default. They default at the point in time at which they go in repayment, to a greater extent than any other time.

I would believe that this program has shown that there is a substantial decrease in defaults through the consolidation program. I would not want to make the claim that it is solely a function of consolidation, whether we can quantify it, but when you are looking at default rates that average between 10 and 12 percent in general, skewed among different populations to be sure and then see a default rate of something less than 1 percent after a conversion period, you have to believe that there has been some substantive decrease in defaults.

Again, I wouldn't want to say how much of that comes about because of our process. We cannot say what that pool of people might have done otherwise, but certainly there has been no experience anywhere else to indicate default rates that low and we hope that we can maintain that.

When we created this program, our goal was to provide maximum participation from the borrower in selecting payment terms, both fixed and graduated, which could be effectively serviced, but which did not present the borrower with a bewildering array of decisions. We believe that we have succeeded in this effort and I have appended to the statement that we have given to you all of the different types of documentation attendant to a loan consolidation.

You will get to see in that just how complex a process it is and this would reinforce your notion that if you do do anything to change the program, that you try to put in place certain standards, certain similarities of delivery mechanisms to make it easier for the students and easier for the people who are participating on the other side—the financial aid officers, the banks and the States.

Just very quickly, we have seen the testimony of Dr. Edward Elmendorf and also the GAO at your meeting a week or two ago. Our recollection was that Dr. Elmendorf made a number of comments relative to the kinds of things in the law of a technical nature which might allow for certain abuses or for certain costs to the Federal Government.

In actuality, over a period of time, we negotiated with the Department to put in place an agreement which protected the Gov-

ernment as well as protected Sallie Mae in putting this program in place so I believe that all of these technical kinds of issues that Dr. Elmendorf was raising can be dealt with between the Department and any others who originate this program.

I don't believe that anybody who gets into consolidation automatically has a license to disavow any sections of the statute or can cause harm unnecessarily. I don't believe the statute is that badly drawn. It is an easy technical matter to deal with either legislatively or dealing on a regulatory basis with the Department.

The question was raised about the interest rate in this program. You may recall that a 7-percent interest rate was mandated in the legislation and subsequently the interest rate for students who are borrowing in GSLP went to 9.

We would support and have supported the notion that if a student has originally gotten his GSL at 7 or at 9 or at 12 or at 14, consolidation should be at that level. This, too, can be corrected through legislation. It has not cost the Government very much to this point because we haven't consolidated any higher yielding loans in the 12 or 14 category and very, very few of the 9-percent loans have actually come into repayment yet, in such a way that they have been eligible for consolidation at 7.

We would hope that you would deal with that in this legislation and I don't think that that's a major problem for any party. I don't think that would be a disincentive for anybody relative to consolidation.

There are also a couple of questions relative to section 427 of the act. It was a specific concern that if we were to make a consolidation loan we had to give the check straight to the student or the graduate and have that individual take the proceeds and pay off the existing loans. That would have put twice the funds into the hands of the borrower and we didn't think that was appropriate.

We did work out something with the Department. They feel they stretched the legislation a bit, but they did work it out so that we could have coendorsement to send it straight to the banking institution. We didn't want to see doubling up of large loans like that. That, too, may have to be addressed with legislation, but it's a relatively simple thing—it's a technical—just to make certain that obvious problems relative to consolidation aren't managed prejudicially to the Government.

Finally, we have seen Mr. Henig's comments from the General Accounting Office. We expect that his full report will be forthcoming. We have not seen it as yet. It is probably due in the next 2 to 4 weeks. But we believe that when you get the final report from the GAO that it will indicate that loan consolidation is a worthy program that Sallie Mae has administered responsibly and fairly and that we have managed it consistent with the original legislation.

I think it will also indicate that there has been no material cost to the Government for having had this particular program in place for the last 18 months. It is not as large a program as people might have expected it to be. In actuality, something less than 1 percent of the people who are eligible for it actually undertake a program of consolidation.

It is turning out to be what we expected it to be. Those who have a need and can utilize to better match their income with their outflow use it. Others just choose not to.

Finally, as you know, has a sunset on July 31 and because it takes 60 to 90 days to consolidate a loan—it's a very complex process—we have begun to notify borrowers that it could conceivably be a problem as of that date. We have indicated to people that it's our understanding that there is good will toward this program on the Hill and it probably will be reauthorized, and that there could be a time gap in there—we hope that there is not—but we asked them to continue the application process, given the complexities of it, and we do hope that in your considerations you do choose to reauthorize it because we think it has provided modest, not necessarily costly service to students and that it has not been abused in any way at the expense of the Federal Government.

Those are my comments, Mr. Chairman.

Mr. SIMON. Thank you very, very much. Let me also welcome a brandnew member to the subcommittee, Tim Penny from Minnesota. We are pleased to have you as a member of the subcommittee.

Mr. PENNY. Thank you, Mr. Chairman.

Mr. SIMON. I was interested in your comment that those who are taking advantage of this are people who really are in need. One of fears has been that consolidation, in fact, is going to be an attractive option for people who really don't have the needs.

Have you done any intensive study to know that that is the case, and let me, just for a moment, be the devil's advocate—if you see somebody who has a default, who has problems, doesn't that become an unattractive to be providing consolidation for?

Mr. FOX. We don't provide consolidation to people who are delinquent or in default. We have decided that somebody has to be in good standing. The reason for that is as much operational as philosophical because the process of curing a default or a deliquency, it means an interaction with the guarantor and the like and it could well be tbat at the point in time in which we are sending a check, a guarantor is sending a check to the lender as well.

But we feel that if a student can be encouraged to get their loans into grace, that they catch up on the default then they can be eligible for the process. But we have made it a policy decision not to consolidate delinquent of defaulted loans.

Additionally, we have worked out a repayment schedule with the Department of Education so that a student can't take a term and then get maximum term under the consolidation which is 20 years. We believe that at certain levels of indebtedness, they should get moderate extension; at a higher level, even more extension as a possibility. In that way we have foreclosed the possibility of egregious cost increase to the Government. Somebody with a $5,000 note can't automatically say, "I'll pay nothing back for 20 years and then pay it the 20th year," which would be the maximum cost to the Federal Government.

We would spread that out and give that person three options, one of which would be no cost increase to the Government, which is a graduated repayment on such a schedule of graduation that the average indebtedness over the timeframe is exactly the same as

it was before. All it does is must moderate the up front payment. So that costs the Government nothing.

The second one, which is graduated repayment, tries to match the income of the student to the payback and, in most cases, that stretches out the loan to maybe 13 or 14 years from a 10-year maximum before, It's only when you get a very large loan, which is probably where your higher incidence of default comes anyway that you give the person the opportunity even to get out close to 15 or 20 years.

I don't think you are going to find that the cost is that great on the interest benefits under the special allowance.

Mr. SIMON. In terms of costs, what are we talking about? You can define them on a per consolidated loan average or however you want to define it. What are we talking if we authorize a major program here?

Mr. Fox. Well, I think you have already authorized it and it hasn't proven to be that large in any case. The issue here is if that program should be shared or diffused in terms of who offers it. But I don't think the program is that much larger we have already defined because we have had nationwide advertisements, as you know, and have sent out publications to millions of eligible people and we just haven't gotten the kind of response that suggest that there are a lot of very heavily indebted students out there who want to use this thing.

But we bear costs certainly as an originator. The cost of outreach, finding the individual, and consolidating. Those are costs borne by Sallie Mae. We get no cost allowance, we don't charge the student an additional insurance premium or anything like that.

The cost to the government is the fact that you are extending the loan and in so doing, you are going to be making interest benefits available, possibly, depending on interest rates, for a longer period of time than otherwise might have been the case.

That might extend the average life of the loan perhaps 30 percent, depending on the conditions under which the student undertakes to extend. The offset to that is, presumably, a lesser amount of operational costs to the different people who are holding those four, five or six notes, which only have to service one. Second, to the extent that you can reduce defaults, those defaults occur early on in the process, that's on offset to the higher interest costs.

If you recall, this program was designed in this way to offer consolidation because they couldn't consolidate all of the programs up front. It was felt that if you had some kind of a screening device, if after the student had graduated, you put in place certain kinds of tests to make certain that only those who have high indebtedness or multiple borrow relationships would only be in the first place, which you could limit. Those tests seem to be working.

I believe that the costs for this are modest. I don't think you are going to be able to document those exact costs for long periods of time——

Mr. SIMON. But can you give us some kind of ball park figure? In other words, if we go ahead and say, "From August 1 on this whole program is reauthorized," what kind of terms are we talking in for fiscal year 1984?

Mr. Fox. Well, the General Accounting Office has indicated that for each $100 million of this, based on certain interest rate assumptions and certain default assumptions, something less than 2 percent of additional cost would be added, roughly $2 million per $100 million. That's in their report, I believe.

We are not in a position to judge what the Federal cost is going to be on this thing. We have not studied it, but don't find that it would be anything—we don't believe it would be materially greater than what the General Accounting Office has suggested.

Mr. SIMON. And then finally—I guess really it's a philosophical question—there are those who would argue the business of Congress and this committee, this subcommittee, is to see that students get to college. Once they get to college, how they handle their loans after that is their business and we shouldn't really be worried about that too much. How do you respond to that?

Mr. Fox. I believe that there has been much greater reliance on credit the last 5 years than anybody had expected. I think that you created a debtor class. You have a generation of people who 10 years ago would have seen their education paid by the moneys saved by their parents and now we have put the burden on these people to get an education, to tap their future earning stream for payment of their education.

To the extent that we can facilitate the repayment without needlessly increasing costs to the Federal Government, giving these people the opportunity to pay back their loans, I think, is a valuable kind of an exercise. These kids are mobile, they borrow in a number of different places. The programs have changed a number of times over the last few years so that they have been required to scratch and bite and try to find debt wherever they could. You have made them eligible for NDSL's or health programs, GSL programs, you have disenfranchised them from time to time, and in order to get through school, we find that those who have multiple borrow relationships, have three or four relationships, three or four guarantees or guarantors, in some cases.

I think that if we can provide a means by which they can facilitate their repayment, we are not giving particular additional costs to the Government and I don't feel we are, and if we can reduce the defaults which seems to be a statistic which people seem to dwell upon in this country, then we have accomplished something. We have done in a way not costing the Government anything, any material amount and it's just facilitating.

The costs of this are borne primarily by the student and by the originator. We do all of the work in trying to locate this person, making them aware of the program that is available and it's a very costly process, much more costly than a normal loan origination.

The student, frequently, is actually going up to a higher interest rate and you are getting your 3 percent money back in your NDSL or whatever, whenever one of the students chooses to go to a 7-percent or a 9-percent loan. So a student is actually choosing to pay a bit more interest for the opportunity to consolidate and better manage their financial affairs.

I really see nothing wrong with it. I really think it's a very positive kind of a program. I really at this point don't see any cost of

any magnitude that should make you squeamish about extending it.

Mr. SIMON. Mr. Gunderson.

Mr. GUNDERSON. Thank you, Mr. Chairman, and thank you, Mr. Fox, for coming before us to discuss one of the more complicated programs we deal with in this subcommitee.

You have said in your statement that if we go to some kind of a national program which allows the States and the lenders to be involved, that you are very concerned it be a uniform program.

What suggestions would you have in that particular area as to how a national uniform should be structured or administered?

Mr. Fox. Well, certainly to the extent that there are policy issues, that would have to come from you, but first, the eligibility requirements are set statute—you might want to amplify on some of those eligibility statutes. Do you want to limit whether people have the opportunity to consolidate if they are delinquent or in default. Right now that is just something that we are working out and it's not something that is specifically in the statute.

Do you want to perhaps mandate repayment terms that would limit against just offering the program so that everybody could convert to a 20-year loan and get the maximum Government subsidy, whether it's needed or not. We have put in place, in consultation with the Department, a schedule that limits the amount extensions somebody could get based on their loan size. That extension is where the cost comes in, because each additional year that loan is on the books, the Government may have to pay an interest benefit on it.

So certain rules relative to how much extension you can give, the eligibility requirements of it—you may wish to look at things like—since these students have loans from more than one guarantor, in many cases, who would be the vehicle of choice to offer the consolidation?

It goes on and on. But these are things that either have to be dealt with through regulation or through specifistic law, but which make it very clear that this not a program to be abused and to offer maximum benefit to anybody that desires it, that it be policeable, that there be reporting requirements, because the Department of Education needs data coming from the originators so that they have an idea of what the old loans, where they came from and the like, because they have a lot of requirements that require analysis.

So solid reporting, origination practices, limitations of costs through certain devices, certain rules relative to eligibility, certain rules relative to perhaps making fees available to people who are not going out and competing and trying to throw money at institutions for converting or whatever—something that gives some aura of consistency, both from the Government's point of view, from cost and from the operational nature of the program.

Mr. GUNDERSON. Do you personally have any feelings as to whether or not we should extend loan consolidation to the States?

Mr. Fox. I have reported to you that if it's a policy issue that we are not going to argue against it. We have said that monopoly is something that is difficult to defend and we would try to defend against monopoly at this time.

M. GUNDERSON. Someone suggested that the present loan consolidation program is one that's very cost effective, no cost at all to the Federal Government. They are not sure that that would happen if we extended the authority. I guess that is one of the big areas of controversy, as to whether or not we would then get into some kind of cost to the Federal Government.

What is your analysis? Do you think if we extend loan consolidation to the States or lenders that there will be a cost incurred to the Federal Government?

Mr. Fox. I don't think that there is any doubt that there is adequate capital available for this program, but I don't think that is the issue. The issue is that there are a number of institutions that have been created to provide service in their geographic district and they want to be able to offer full service and feel that they should have the opportunity to provide that service in their jurisdiction.

I can't argue that. I think that the costs that you have to deal with are administrative costs to the Federal Government, certain redundancies that might come about in terms of cost of putting these programs in place. We are not talking about a very large program here. People keep thinking that we are talking about a multibillion dollar thing and it just hasn't happened, and I don't think that we have found a single State where there's any very large amount of these loans proportionate to their pool.

But there are going to be costs of administration at the local level to do it right, the cost of reporting, which are redundant. I think you are going to find that there are administrative costs and regulatory costs to the Federal Government and certainly there is the cost associated with the revenue. What those amounts are are being analyzed by others and I would look to the Department of Education to tell you what they think the administrative costs would be.

I have no doubt that the States, or any others for that matter, if they so desired, could put this program in place—I don't believe they have got it yet—but they could put it in place and it would be a fine type of program.

But I think there are costs. I think you have already decided in the past that those costs would not inhibit you from other programs.

Mr. GUNDERSON. Finally, do you project any need in the near future to raise the interest rate on consolidated loans?

Mr. Fox. I think that there are a number of students who will be coming into the progress in the next. few months, let alone the next few years, whose borrowing has been at 9 percent. It would be inappropriate for those to get an additional subsidy, which would be mandated under the existing programs.

We created a program with a 7-percent interest rate and the same legislation created a new type of borrower at a new rate and I don't believe it was intentional. There has been some speculation that the 7-percent rate was meant to be an inducement for some low consolidate. I don't believe that was the intent at all. It was to give people an opportunity to manage their affairs and not to give them additional subsidy.

You also have the possibility of other rates associated with parent loans, last loans, the like, and I think that anybody who's borrowed should have a refinancing fairly at the terms at which they originally borrowed. This is an accommodation. It's not a subsidy program. And I would be strongly in favor of reworking the legislation in that way.

Mr. GUNDERSON. In the absence of the Chair, he has asked that I continue the hearing, and we'll do so by calling Mr. Penny.

Mr. PENNY. I have no questions.

Mr. GUNDERSON. Mr. Packard.

Mr. PACKARD. Thank you, Mr. Chairman.

I appreciate the testimony of Mr. Fox. Following up on the question regarding interest, would it be feasible to consider tying that with the prime rate, like many of our current lending institutions are with regular conventional financing?

Mr. FOX. Well, prime rate is a curious phenomena. Very few people seem to be borrowing at prime anymore. It seems to be more of a memo figure from the banking system to give an indication more of direction of rates more than anything else. We have found over the last few years in trying to find ways in which we might tie the student loan to some kind of a rate, that——

Mr. PACKARD. By that I meant a variable rate, then rather than tying it directly to prime rate. Some formula that would give it a variable rate that would relate to the fluctuations of a true interest rate.

Mr. FOX. We have found that relating the student loan to the cost of funds of the institutions was better than trying to relate it to prime which is with their lending rate. Last year alone, for example, we have seen—for the last 2 years we have seen prime anywhere from 10 to about 22 percent.

When currently prime is 10½, I think a student loan is yielding somewhere around 12½ today. When prime was at 22½ a student loan was yielding around 17, significantly below the prime rate. We have found that there would be less volatility in the rate with the T-bill as opposed to prime and since what we are trying to do is insure that those who lend in this program and borrow their funds in the short-term environment, have some kind of a yield on their loans that moves pretty much with their cost of funds, and that was best done if you tied it to the Treasury bill plus some kind of an increment. It's also a number that is created every week through an actual auction rather than being some memo figure that the bank posts arbitrarily.

It is something which is dependable, something on which the banking has come to depend upon in terms of the yield in this program. This program does not yield anywhere near as much as traditional consumer loans, but it is more predictable, which is very useful to lenders.

Mr. PACKARD. Generally speaking, does the banking industry seek out these kinds of loans or are they doing them to accommodate and serve a need?

Mr. FOX. Well, you know, I think we have gone through a very dramatic change, Congressman; 10 or 15 years ago when the program was a more embryonic stage, yields were lower, changes were sometimes relatively thoughtless relative to operations and the

like. Banks were doing this as a lost lender and because the American Banking Association and others said, "This is something that is appropriate for you to do." Lending was very modest. There was not access and I can tell you that most banks lost money on this thing and were doing it as a public service.

But over the years there has been much more concern about the operational aspects of the program and the legislation that comes out of here. The loan has been indexed in a way that at least gives some assurance that they are not going to be whipsawed if the interest rates move up or down because you know in the old days the rate was set quarterly by a committee; there was no formula.

So by having indexed the instrument, by having more attention to detail, by having the program decentralized to the States and getting closer surveillance and management of the program on a State-by-State basis, improving the timeliness of payments from the Federal Government by putting the penalty burden on the Government if they didn't pay on time—all of these things have made lenders much more willing to participate in the program.

What has also happened is now you have a number of institutions who are willing to make loans on a nationwide basis. There is no shortage of private capital in support of this program right now, which is a marked change from just 5 or so years ago.

The gentleman who is going to testify after me represents one such institution where there is a willingness to make loans of last resort around the country. This becomes a part of their strategy for interstate banking to try to get clients all over the country. So it works.

Mr. PACKARD. Very good. Do you see any group of people, minorities or poor people or any specific groups of people, that are not being served by this procedure? Is it available to everyone and does it really serve the total needs that are out there?

Mr. FOX. There was a provision in my law that said that we could not deal with anybody who denied access to a loan for reasons of race, sex, religion, and the other EEOC kinds of things. It also said that you could not do business with Sallie Mae if you required a prior business relationship with the institution.

We are pleased that we have been a part of a process over the past 10 years where banks have stopped that kind of provision in most parts of the country and we think that it was our legislation that germinated here, which, to a great extent, pushed that.

There may be isolated pockets where small groups don't get access to the program, but if they can be identified, we believe that there are others who will make loans available to them. We hear very infrequently of people who claim that they don't have access.

We did hear a week or two ago testimony from former Under Secretary Clohan that prospective small borrowers, those who borrow very small amounts, have difficulties getting loans. That, I believe, is a cost problem associated with the banking industry today which is passing through the costs associated with high yielding deposits, in terms charging for service and small loans just don't pay the freight. For us, the high cost of servicing for small loans doesn't pay the freight.

So if anybody is being disenfranchised, it would seem to be the very small prospective borrower, who may not have to borrow at

all. I think that the last hearing suggested that reauthorization deal with that and I know there are groups of people now, based on that hearing, that are trying to address that issue.

Mr. PACKARD. Thank you.

Mr. GUNDERSON. Are there any other questions?

[No response.]

Mr. GUNDERSON. If not, thank you again very much, Mr. Fox, for your testimony and for your cooperation. All of us, I suspect, will be talking to you again either informally or formally before we complete this process.

With that, we call our next witness, which is Stephen Biklen, vice president, Citibank.

[Prepared statement of Stephen Biklen follows:]

PREPARED STATEMENT OF STEVE BIKLEN ON BEHALF OF THE AMERICAN BANKERS ASSOCIATION

Mr. Chairman and Members of the Subcommittee I am Steve Biklen, Vice President in charge of Citicorp's student loan business and repersent the American Bankers Association.

Our Association's membership includes more than 90 percent of the nation's full service banks. While our members range in size from the smallest to the largest banks, approximately 90 percent of them have less than $100 million in assets.

I am pleased to be here today to discuss the United States General Accounting Office Report on the Student Loan Marketing Association's (Sallie Mae's) loan consolidation program. The extension of the consolidation program is of interest to lenders with respect to the cost impact it may have on the guaranteed student loan program and the effect it may have on lenders to the extent that they are not able to offer loan consolidation if they wish. The ABA believes strongly that the ability of lenders to offer loan consolidations would greatly simplify administration of the program, particularly in those situations where all of the loans to be consolidated are held by one lender.

The American Bankers Association has been asked to comment specifically on the May 25, 1983, report of the GAO, and as such our comments will primarily address points relating to private lenders.

As noted on pages 1 and 2 of the GAO report, Sallie Mae has an exclusive franchise to provide consolidated loans to student borrowers. This places private lenders, who intend to hold student loans during the repayment period, at a serious competitive disadvantage. For example, Sallie Mae can purchase the more profitable higher balance loans while private lenders cannot compete on an equal basis.

Page 2 of the report notes that as of December 31, 1982, Sallie Mae had consolidated 10,648 loans totaling $66.9MM from 5,473 borrowers. It would be useful to know the breakdown of these consolidated loans in the following ways: Number of loans from the same lender, same guarantor, number of loans from same lender, different guarantors, number of loans from different lenders, different guarantors.

We believe that such information might substantiate the need for private lender participation in the consolidation program.

As a point for clarification pages 2 and 3 compare the monthly payments for consolidated loans versus nonconsolidated loans. The report notes that a borrower with nonconsolidated loans would pay $166 per month for 10 years while the borrower with a comparable consolidated loan would pay $96 for 16 years. These numbers appear inconsistent because the total payments of the consolidated loans would be less than the unconsolidated loan as follows:

Unconsolidated:	
Monthly payment (multiplied)	$166
Number of years (multiplied)	10
Months (multiplied)	12
Total payments	$19,920
Consolidated:	
Monthly payments (multiplied)	$96
Number of years (multiplied)	16

Months (multiplied)	12
Total payments	$18,432

Logic would dictate that the total of the payments over 16 years should be greater than the total of the payments over 10 years. This point should be clarified.

Another point to be made is that while the consolidation program will reduce a borrower's monthly payments, the total to be paid back by the borrower will be substantially increased. This is demonstrated by the following schedule:

Finance charge at 7 percent for $7,500 borrowed for the term indicated:

10 years	$2,950
15 years	4,634
20 years	6,455

Page 3 notes that Sallie Mae estimates that the consolidation program will cost the Federal government an additional $2 million for every $100 million of loans consolidated. Assuming that the consolidation rate remains at 7 percent, we would expect that the cost to the federal government will increase over time, simply because the larger portion of the loans being consolidated will carry a 9 percent interest rate and, therefore, the cost of the special allowance will increase when the rate is reduced to 7 percent. Therefore, we recommend that the Congress consider increasing the 7 percent rate in order to reduce the cost of the program to the federal government.

The bottom of page 3 notes that Sallie Mae used a conservative 2 percent default rate in its assumptions for consolidated loans. Based upon input from state guarantee agencies, it is our understanding that over 50 percent of total defaults result from first-time payment defaults. Additionally, the consolidation program appeals to those borrowers who are most interested in repaying their loans. Based upon these underlying assumptions we agree that a two percent default rate looks conservative. This is further supported by the narrative on page 4 of the GAO report which notes that the annual default rate for the guaranteed student loan program is 10 percent. Here again we understand that over half of this rate is due to firt-time payment defaults.

The ABA agrees with the Department of Education that the consolidation default rate cannot be compared to the normal guaranteed student loan default rate or NDSL default rate. It would be very meaningful, however, to understand what the average stage of repayment was for those loans that Sallie Mae has consolidated to date, and compare that to the default rate for GSL loans at the same stage of repayment. If such information can be obtained, an accurate assessment of the impact of the consolidation program on default rates could be made.

Page 5 of the report begins a discussion of the various program alternatives as seen by the GAO. We would like to comment on these alternatives as follows:

Extending loan consolidation authority to State programs

The GAO considered extending the consolidation program to states but did not consider extending it to private lenders operating in the guaranteed student loan program. The ABA supports extension of the authority to make consolidation loans to all private lenders in the guaranteed student loan program. These private lenders are making student loans today and many of them hold the loans as they move from the in-school phase into repayment. If a student has more than one loan, the lender normally consolidates those loans into one loan for the repayment period. Thus lenders have experience in this consolidation process. Additionally, the ABA favors lender particpation in the consolidation program, particularly in the instance where the loans being consolidated are held by one lender, or by two lenders under the same guarantee program. The administrative process of consolidating the loans would be greatly simplified, becasue there would be fewer parties involved. It would not be necessary to call upon another party such as Sallie Mae or the State secondary market to become involved in the transaction. The concept of having lenders particpate in the consolidatioin program is further supported by Sallie Mae's finding (noted on page 12) that 93 percent of loans consolidated were under the GSL program.

Pages 10 and 11 of the GAO report discuss issues relative to the administrative cost allowance [ACA] and insurance premiums. Allowing private lenders to offer the consolidation product would contribute to the resolution of these issues and would probably result in reduced cost to the federal government. We would recommend the following:

Same lender, same guarantor.—Lender would consolidate the loans using the same guarantee. There would be no need for the ACA or insurance.

Same lender, different guarantor.—The loans could be insured directly by the Department of Education as Sallie Mae does now, or a guarantor could opt to insure the total consolidated loan with no ACA or additional insurance.

Different lender, different guarantor.—These loans could be consolidated by the lender and insured directly by the Department of Education as Sallie Mae does now. There would be no need for ACA or additional insurance.

Averaging interest rates

We agree with the conclusion of Sallie Mae and most state programs that the capability to determine the consolidated loan interest rates on an average or weighted basis could be implemented, but that this process would cause severe administrative problems with the special allowance billing. To alleviate this situation, the ABA recommends that either one rate, say 8 percent or 9 percent be used, or that the borrower's GSL rate be the determinant of the consolidated rate. For example a borrower with a 7 percent GSL would obtain a 7 percent consolidated rate. A 9 percent borrower would obtain a 9 percent consolidated rate. Implementation of either of the recommendations would reduce the cost of additional special allowance to the government.

Revising qualifying loan amounts

Here again the ABA recommends simplicity and perhaps raising minimum qualifying amounts and limiting the repayment terms to help hold down the cost to the government. Rather than using many different repayment schedules, we recommend a simple table of options such as the following:

Consolidated loan amount:	*Maximum maturity (years)*
Over $7,500	10
Over $10,000	12
Over $15,000	15

Page 15 of the GAO report discusses situations where the borrower may not qualify for consolidation, but may have several loans and, therefore, be paying several minimum payments. The concept of allowing lenders to participate in the consolidation program would help alleviate this situation particularly where the loans involved were guaranteed student loans. The lender could simply consolidate the borrower's loans at the original rate of the loans, which would have to be either 7 or 9 percent, and keep the repayment terms to a maximum of 10 years. This would reduce the borrower's monthly payments because the effect of applying the minimum loan payment to several loans is eliminated.

As a point for clarification page 14 notes that lenders would usually require at least the $50 minimum monthly payment for GSL's due to loan servicing costs. It should be noted that the minimum $50 payment is not subject to lender option but is required by law.

Eliminating the special allowance on consolidation loans

The ABA agrees that the special allowance on the NDSL portion of the loans should not be eliminated. Elimination of the special allowance for NDSL loans would give little incentive for anyone to consolidate those loans. Additionally, NDSL loans comprise only 7 percent of the total loans being consolidated and therefore, would have a relatively small impact on the total cost of the program.

Summary

In summary, the ABA strongly recommends that private lenders be allowed to participate in the consolidation programs. They are an integral part of the guaranteed student loan program, and they have experience in consolidating loans today. Inclusion of private lenders would greatly simplify the consolidation process by eliminating the need for another party, such as Sallie Mae or a state agency, to get involved in administratively processing the loans.

Second, the ABA strongly recommends that the consolidation program be kept as simple as possible. The rate structure should be simplified and use of a higher rate than 7 percent would help defray the cost of the program. The repayment terms should be kept to a minimum of 3 or 4 options rather than a sliding scale. This would greatly simplify the administration of the program and result in a better understanding of it by those who benefit from it most, the borrowers.

Thank you very much for the opportunity to comment on the consolidation program at this hearing. If you have any questions, I would be more than happy to answer them.

STATEMENT OF STEPHEN C. BIKLEN, VICE PRESIDENT, CITIBANK (NEW YORK STATE), N.A.

Mr. BIKLEN. Mr. Chairman, members of the subcommittee, I am Steve Biklen, vice president in charge of Citicorp's student loan business and represent the American Bankers Association.

Our association's membership includes more than 90 percent of the Nation's full service banks. While our members range in size from the smallest to the largest banks, approximately 90 percent of them have less than $100 million in assets.

I am pleased to be here today to discuss the U.S. General Accounting Office report on the Student Loan Marketing Association's [Sallie Mae's] loan consolidation program. The extension of the consolidation program is of interest to lenders with respect to the cost impact it may have on the guaranteed student loan program and the effect it may have on lenders to the extent that they are not able to offer loan consolidation if they wish.

The ABA believes strongly that the ability of lenders to offer loan consolidations would greatly simplify administration of the program, particularly in those situations where all of the loans to be consolidated are held by one lender.

The ABA has been asked to comment specifically on the May 25, 1983, report of the GAO, and as such, our comments will primarily address points relating to private lenders. As noted on pages 1 and 2 of the GAO report, Sallie Mae has an exclusive franchise to provide consolidated loans to student borrowers. This places private lenders who intend to hold student loans during the retainment period at a serious competitive disadvantage.

For example, Sallie Mae can purchase the more profitable, higher balanced loans while private lenders cannot compete on an equal basis.

Page 2 of the report notes that as of December 1982, Sallie Mae had consolidated 10,648 loans totaling $66.9 million from over 5,000 borrowers. It would be useful to know the breakdown of these consolidated loans in the following ways: The number of loans from the same lender and the same guarantor; the number of loans from the same lender, different guarantor; the number of loans from different lenders and different guarantors.

We believe that that information might substantiate the need for private lender participation in the consolidation program.

There were two other points for clarification in the report. One dealt with a schedule in there that indicated that a borrower with nonconsolidated loans would pay $166 per month for 10 years while the borrower with a comparable consolidated loan would pay $96 for 16 years. Those numbers appeared inconsistent to us in the sense that the total payment to the consolidated loans would be less than the unconsolidated loan as follows: The unconsolidated loan amount to total payments of $19,920 over the 10-year period whereas the consolidated loan amounted to $18,432.

Logic would dictate the total of the payments over the 16 years would be greater than the total of payments over the 10 years. We think that point should be clarified.

Another point to be made that was not brought out in the report is that while a consolidation program would reduce the borrower's

monthly payments, the total to be paid back by the borrower will be substantially increased so that if you have a 7-percent loan of $7,500 the finance charge over 10 years would be $2,950 and over the 10-year period it would be over $6,000.

Page 3 notes that Sallie Mae estimates the consolidation program would cost the Federal Government an additional $2 million for every $100 million of loans consolidated. Assuming that the consolidation rate remains at 7 percent, we would expect that the cost to the Federal Government will increase over time, simply because you will have more of the 9-percent loans going into consolidation. Therefore, we recommend that the Congress consider increasing the 7-percent rate in order to reduce the cost of the program to the Federal Government.

The bottom of page 3 notes that Sallie Mae used a conservative 2-percent default rate in its assumptions for consolidated loans. Based upon input from State guarantee agencies, it is our understanding that over 50 percent of total defaults result from first-time payment defaults. Additionally, the consolidation program appeals to those borrowers who are most interested in repaying their loans.

Based upon these underlying assumptions, we agree that a 2-percent default rate looks conservative. This is further supported by the narrative on page 4 of the report, which notes that the annual default for the guaranteed student loan program is 10 percent. Here again we understand that over half of this rate is due to first-time payment defaults.

The ABA agrees with the Department of Education that the consolidation default rate cannot be compared to the normal guaranteed student loan default rate or the NDSL default rate. It would be very meaningful, however, to understand what the average stage of repayment was for those loans that Sallie Mae has consolidated to date, and then compare that to the default rate for GSL loans at the same stage of repayment. If such information can be obtained, an accurate assessment of the impact of the consolidation program on default rates could be made.

The report begins a discussion of various program alternatives as seen by the GAO. We would like to comment on these alternatives as follows:

The first alternative was extending loan consolidation authority to State programs. The GAO considered extending the consolidation program to States but did not consider extending it to lenders. The ABA support extension of the authority to make consolidation loans to all private lenders in the program. These private lenders are making student loans today and many of them hold the loans as they move from in-school into repayment.

If a student has more than one loan, the lender normally consolidates those loans into one loan for the repayment period. In this way, lenders have experience in the consolidation process today. Additionally, the ABA favors lender participation in the consolidation program, particularly in the instance where the loans being consolidated are held by one lender or by two lenders under the same guarantee program.

The administrative process of consolidating the loans would be greatly simplified because there would be fewer parties involved. It

would not be necessary to call upon another party such as Sallie Mae or the State secondary market to become involved in the transaction.

The concept of having lenders participate in the consolidation program is further supported by Sallie Mae's finding that 93 percent of loans consolidated to date were under the GSL program.

Pages 10 and 11 of the GAO report discuss issues relative to the administrative cost allowance, the ACA, and insurance premiums. Allowing private lenders to offer the same consolidation product would contribute to the resolution of these issues and would probably result in reduced costs to the Federal Government.

We would recommend the following in the situation with the same lender, same guarantor. The loans would simply be consolidated. There would be no need for ACA or insurance.

In the situation of the same lender, different guarantor, the loans could be insured directly by the Department of Education as is done now with Sallie Mae, or a guarantor could opt to insure the total consolidated loan with no ACA or additional insurance.

In a situation of different lenders, different guarantors, those loans could also be consolidated by the lender and insured by the Department and there would be no need for ACA or additional insurance.

On the issue of averaging interest rates, we agree with the conclusion of Sallie Mae and most State programs that the capability to determine the consolidated loan interest rates on an average or weighted basis could be implemented, but that this process would cause severe administrative problems with respect to the special allowance billing.

To alleviate this situation, the ABA recommends that either one rate, say 8 percent or 9 percent be used, or that the borrower's GSL rate be the determinant of the consolidated rate.

For example, a borrower with a 7-percent GSL would obtain a 7-percent consolidated rate. A 9-percent borrower would obtain a 9-percent consolidated rate. Implementation of either of those recommendations would reduce the cost of additional special allowance to the Government.

In terms of revising the qualifying loan amounts, here again, the ABA recommends simplicity and perhaps raising minimum qualifying amounts and limiting the repayment terms to hold down the cost to the Government. Rather than using many different repayment schedules, we would recommend a simple table such as, over $7,500, the maximum maturity might be 10 years. Over $10,000, 12 years and over $15,000, 15 years.

Page 15 of the GAO report discusses situations where the borrower may not qualify for consolidation, but may have several loans and, therefore, be paying several minimum payments. The concept of allowing lenders to participate in the consolidation program would help alleviate this situation, particularly where the loans involved were guaranteed student loans. The lender could simply consolidate the borrower's loans at the original rate of the loans, which would either be 7 or 9 percent, and keep the repayment terms to a maximum of 10 years. This would reduce the borrower's monthly payments because the effect of applying a minimum loan payment to several different loans would be eliminated.

As a point of clarification page 14 notes that lenders would usually require at least the $50 minimum monthly payment for GSL's due to loan servicing costs. It should be noted that the minimum $50 payment is not subject to lender option but is required by law.

On the subject of eliminating the special allowance on consolidation loans, the ABA would agree that the special allowance on the NDSL portion of the loans should not be eliminated. Elimination of the special allowance for NDSL loans would give little incentive for anyone to consolidate those loans and, additionally, the NDSL loans comprise only 7 percent of the total loans being consolidated and therefore, would have a relatively small impact on the total cost of the program.

In summary, the ABA strongly recommends that private lenders be allowed to participate in the consolidation programs. They are an integral part of the guaranteed student loan program, and they have experience in consolidating loans today. Inclusion of private lenders would greatly simplify the consolidation process by eliminating the need for another party, such as Sallie Mae, or a State agency, to get involved in administratively processing the loans.

Second, the ABA strongly recommends that the consolidation program be kept as simple as possible. The rate structure should be simplified and use of a higher rate than 7 percent would help defray the cost of the program. Repayment terms should be kept to a minimum of three or four options rather than a sliding scale. This would greatly simplify the administration of the program and result in a better understanding of it by those who benefit from it most, the borrowers.

Thank you very much for the opportunity to participate in this hearing. I would glad to answer any questions you might have.

Mr. GUNDERSON. Thank you for your testimony.

The chairman of the committee said at this point in time we would insert in the record a letter from you and the chairman's reply. I think it was dated May 16, and without objection that will be inserted in the record.

With that, we call on Mr. Penny.

Mr. PENNY. Maybe you don't have this information. I am curious to find out the relationship between private lenders and State lenders in the student loan field and approximately how much of the need is being met by private financial institutions.

Mr. BIKLEN. I don't have the numbers available, but I think basically the relationship is such that in a number of States, private lenders provide the capital needed to meet the demand for student loans.

In a number of other States, that capital has not been adequate and we have seen the State bonding authorities fulfill that need in a sense that they come in as a secondary market, buy the loans from the originating lender and then the lender in turn would be free and would have capital free up to make additional loans.

I don't have access to the numbers involved at this point.

Mr. PENNY. Could you run through again for me the approach you would like to see applied for determining an interest rate on a consolidated loan?

Mr. BIKLEN. We have one of two recommendations. One would be simply changing the consolidation rate from 7 percent to a higher

rate, say 8 percent or 9 percent, and that would help to reduce the additional cost or special allowance to the Federal Government.

An alternative would be to tie the consolidation rate to the rate of the guaranteed student loan that it was being consolidated with, which would either be 7 percent or 9 percent and that would avoid the situation where you would be taking a 9-percent loan down to 7 percent and then causing the special allowance payments to increase over time.

Mr. PENNY. So the second recommendation is just to leave it at the level of the GSL instead of averaging it perhaps with other loans that might——

Mr. BIKLEN. Well, right now all loans that are consolidated would go into one loan that would carry at 7 percent. We would recommend that instead of doing that, if they had a 9-percent GSL, they would consolidate it at 9 percent.

Mr. PENNY. They do that at 9 percent. I have no further questions.

Mr. GUNDERSON. Mr. Blakey, the majority counsel.

Mr. BLAKEY. You mentioned in your testimony, Mr. Biklen, I think on page 5, that some private lenders already are consolidating loans. My question is, are they simply consolidating in a more practical sense, that is, putting the loans together, or are they, in fact, initiating a complete new instrument?

Mr. BIKLEN. Well, in the sense that loans are already on the books of the lender, they are putting those together, but they are putting them into a new instrument that results in one loan which now has a repayment schedule that has to be negotiated with the borrower.

Mr. BLAKEY. Have you estimated at all how much it would cost, for example, Citibank, to implement a consolidation program along lines similar to the one that Sallie Mae is now pursuing?

Mr. BIKLEN. No, I have not. There would be some additional cost involved, obviously, but we have not estimated what that cost would be.

Mr. BLAKEY. And finally, your testimony is directed almost exclusively to the guaranteed student loan program. Under present law, both national direct student loans as well as HEAL loans also can be consolidated, although no HEAL loans are being consolidated. Would you have any difficulty, if, in addition to the current GSL loans, also national direct student loans and auxiliary loans that were made to graduate or undergraduate students as opposed to parents were also included in consolidation.

Mr. BIKLEN. I don't have any difficulty with that.

Mr. BLAKEY. Thank you.

Mr. GUNDERSON. Sure. Mr. Biklen, as I listened to your testimony and as I read it over, correct me if I am wrong, do you seem to suggest that we could, if we extended consolidation authority to lenders, use you in lieu of Sallie Mae and, in essence, replace Sallie Mae?

Mr. BIKLEN. No.

Mr. GUNDERSON. Or do you see a role for Sallie Mae even with the consolidation authority?

Mr. BIKLEN. Yes. I am not suggesting that they would replace Sallie Mae or the States. I am just suggesting that they would be

providing the service in addition to Sallie Mae and the States, if they are also included.

Mr. GUNDERSON. You indicate that the ability of lenders to offer loan consolidation would greatly simplify the administration of the program. Would you like to elaborate on what you foresee as how we would achieve that?

Mr. BIKLEN. Yes. I am talking about the situation where the loans to be consolidated, where, say, the student had all of those loans with one lender or with two or more lenders operating under the same guarantee program or even operating under different guarantee programs.

But basically what you are doing is you are keeping the whole process with a lender that's already got one of the loans. So you are not having to bring in an additional party, and that's why I think it would be administratively simpler.

Mr. GUNDERSON. Do you think in a situation where we extended this consolidation authority to a lender, that in order to participate in consolidation of loans, there should be some kind of tie-in, should at least one of the original loans ought to be held by that particular lender or ought that not be a requirement?

Mr. BIKLEN. I don't know that that would necessarily be a requirement. I think it would make it easier for the students to do that and they would probably opt to do that anyway. I don't know that you would have to make that a requirement.

Mr. GUNDERSON. You don't think there would be any problem or any incentive one way or the other with a financial institution as someone coming in not having original loans with that particular financial institution in getting that financial institution to participate?

Mr. BIKLEN. No; I think that if that happened though you would have the same situation where now you have brought in another party that was never part of it. But other than that, I don't think it would necessarily have to be a requirement.

Mr. GUNDERSON. If States and lenders were given consolidation authority and in addition to that, we allowed consolidation of loans across State lines, would you foresee any problems in the various State agencies or private lending agencies in perhaps dealing with the different criteria, interest rates, et cetera, in that situation or not?

Mr. BIKLEN. I think there would be an issue in terms of the insurance premium. If you had a State guarantee agency that was now consolidating loans that had previously been guaranteed by another agency, I think that's an issue that needs to be addressed.

We suggested a solution to that. Either they would accept these additional loans without additional insurance or the loans would be insured by the Department of Education and there would be no need for an additional insurance premium.

There would be some—in the case of going across State lines, and operating with different guarantors, the different guarantors do have different requirements, but that's the situation we have today that Sallie Mae would have to deal with when they are consolidating loans from different guarantors. So other than having additional parties that would have to deal with that situation, it wouldn't be any more difficult, I wouldn't think.

Mr. GUNDERSON. One of the criticisms we have heard previously of Sallie Mae is that they take all the, frankly, the big loans and leave all the private lenders with a whole series of small loans that you really can't do much with in terms of investment or anything like that.

Yet, in your statement, you recommend raising the minimum qualifying amounts. First, Do you have any suggestions, as to what the minimum amount should be. Second, I guess I am a little curious that the ABA is proposing that for consolidation because I have heard that's one of the contentions from the other side from the financial institutions.

Mr. BIKLEN. Yes; the recommendation for possibly raising the minimum amount is simply aimed at helping out on the cost side of the equation, helping out the Federal Government so you don't have everyone consolidating loans.

Getting back to your original point, that is very true and I think that is a major point that the ABA is making in that we are being put in a position here where we can't offer the product, but the loans that we wind up selling are the largest loans and that fact remains that it costs the same to service one of those as it does much smaller loans.

We are losing the bigger loans and that's why we would like to be able to offer the service as well.

Mr. GUNDERSON. Do you have any idea of the participation of banks that would occur if we provided this consolidation authority?

Mr. BIKLEN. No, I don't. I have talked to a number of other lenders and I know that they have serious concerns about the number of loans they are selling. I don't know how many banks would ultimately wind up participating in this, although I would suspect that you would have participation in most states by a certain number of lending institutions.

In terms of lending institutions that might do it across State lines, I just couldn't answer that. I don't know I think the larger institutions probably would.

Mr. GUNDERSON. OK.

Do you have any other comments that you would like to make?

Mr. BIKLEN. No.

Mr. GUNDERSON. Thank you very much for your testimony and participation.

At this time we would like to call the panel and I am going to ask that they all come up at once. First of all, Paul Borden, executive director of Kentucky Higher Education Assistance Authority; John Madigan, the executive director, Rhode Island Higher Education Assistance Authority; Roy A. Nicholson, executive director, Indiana Secondary Market for Education Loans, Inc.; and Douglas R. Seipelt, director, guaranteed student loan program, Colorado.

If anybody has a preference, fine. Otherwise we'll just go down the list as your names are called, present testimony and we will withold questioning until all of you have submitted your statements.

As is always the case, your entire statements will be made a part of the record. If you choose to summarize feel free to do so.

Go ahead, Mr. Borden.

[Prepared statement of Paul Borden follows:]

PREPARED STATEMENT OF PAUL P. BORDEN, EXECUTIVE DIRECTOR, KENTUCKY HIGHER EDUCATION ASSISTANCE AUTHORITY, AND EXECUTIVE DIRECTOR, KENTUCKY HIGHER EDUCATION STUDENT LOAN CORP.

Mr. Chairman and Members of the Committee, I am very pleased to have this opportunity to appear before you today to discuss the several issues relating to loan consolidation. As you know from my prior testimony before this subcommittee, I have long been interested in the agencies which I represent having the capability to participate in loan consolidation services now extended under Federal Law only to the Student Loan Marketing Association. My interest in this additional authority is directly related to our efforts to provide comprehensive student loan benefits to all Kentucky qualified residents and to residents of other states who choose to pursue postsecondary education in Kentucky. We now have in place the necessary administrative structure to insure loans, to make direct loans to students who cannot receive such benefits from private participating lenders and to provide loan purchasing (i.e., liquidity benefits) to 257 private lenders now participating within the Commonwealth. I believe until such time as all guarantee agencies and state or local secondary markets are afforded access to the loan consolidation program on terms comparable to those now enjoyed by Sallie Mae that such agencies will be operating at a competitive disadvantage which threatens their continued capability to exist.

In your invitation to appear before the Subcommittee, you identified three points to be addressed. The balance of my remarks are organized around those three points followed by limited comment upon the General Accounting Office report presented to you on May 25.

1. Kentucky's ability to consolidate student loans.—The General Accounting Office [GAO], in its testimony before the Subcommittee on May 25, 1983, concluded that the states have or could obtain the necessary administrative and technical capability to operate a loan consolidation program. I agree with the GAO conclusion. With respect to Kentucky, the guarantee agency [KHEAA] operated as a direct lender under the federally insured program from 1974 until the fall of 1978. During that period, KHEAA developed extensive data processing capabilities for the lending, billing and collection functions. In anticipation of becoming a guarantee agency, KHEAA substantially modified the original servicing system so that by the fall of 1978 computer software was available for all functions relating to the insurance of student loans. Included within the current data processing system is the capability to handle multiple interest rates and multiple loan repayment terms. KHEAA is, in fact, currently administering, on this system, consolidated repayments of students who have both federally insured and state insured student loans. KHEAA has, at various times, provided National Direct Student Loan collection services to an educational institution in the Commonwealth. The system also contains the necessary structure to generate purchase disbursements to holders of loans which would be consolidated and already computes repayment schedules on the basis of all of the notes for any borrower currently within the system. The only significant missing item within the current system is the capability to generate graduated repayment schedules similar to those currently offered in the Sallie Mae Options program. KHEAA certainly has the technical capability to develop such repayment plans promptly following any extension of authority to utilize them. Although the current data processing system is capable of loan consolidations, we have, during the past two years, developed a new generation student loan servicing system which will be completely operational by the end of this year. We are already administering the new Auxiliary Loan Program on this system. This new processing system contemplates the availability of loan consolidation authority and will fully satisfy any who take the time to examine it that the capability to effectively offer consolidation services new exists with the Commonwealth of Kentucky.

2. Desirability of agency consolidating student loans.—The current situation in which Sallie Mae consolidates loans held by other lenders throughout the nation leaves other holders at a substantial competitive disadvantage. Dependent upon the long term success of the Options program, this advantage could cause severe financial difficulties for other large holders of student loan portfolios. Additionally, to the extent Sallie Mae consolidates loans through prepayment of loans held in portfolios financed by tax exempt securities, there is a substantial increase in the net cost of those loans to the Federal Government. This net increase is apparent in the following table:

	Return on 7 percent loans held by Sallie Mae	Return on post Oct. 1, 1980, 7 percent loans held by tax exempt entities	Increased special allowance payments by the Federal Government resulting from Sallie Mae acquisition of a tax exempt financed loan
Quarter ending:			
December 31, 1981	15.92	11.46	4.46
March 31, 1982	17.06	12.03	5.03
June 30, 1982	16.46	11.73	4.73
September 30, 1982	13.36	10.18	3.18
December 31, 1982	11.75	9.50	2.25
March 31, 1983	11.88	9.50	2.38

The average increase in special allowance payments on acquisitions from tax-exempt holders from the inception of the Sallie Mae program in December, 1981 through March 31, 1983 is 3.66 percent. The General Accounting Office report fails to discuss this increased cost. Perhaps, the failure is predicated upon an assumption that the acquisition by Sallie Mae causes the tax exempt security to be retired. The vast majority of student loans financed through tax exempt securities in recent months have utilized short-term instruments (i.e., three to five years) backed by Sallie Mae commitment agreements or commercial bank letters or lines of credit or commitment agreements. Generally speaking, these issues do not contemplate retirement of obligations prior to the stated maturity. Consequently, the acquisition of such a loan by Sallie Mae results in the Federal Government covering both the revenue losses associated with issuance of the tax exempt security and increased special allowance payments associated with loans held by Sallie Mae. An additional and related exposure for lenders, such as Kentucky's Student Loan Corporation, is that a highly successful Options program will increase the risk associated with special redemption through unanticipated prepayment of loans. One of the principal fears of investors in student loan securities is that special redemption calls will occur prior to the stated maturity. This fear is directly related to the fact that student loan bonds are very similar to housing authority bonds. In the housing industry, mortgages, over the past few years, have been prepaid at rates exceeding 80 percent and, as a result, many of these bonds have been redeemed early. The housing industry problems are best explained in terms of interest rate risk and should not be equated to the statutorily set interest rate market in which we operate. The unfortunate reality is that this fear of special redemption is affecting the marketability of student loan securities and the emerging significant volumes of the Options program loan consolidations will tend to exacerbate these fears. Another serious concern is the effect that the options program will have on the average loan balance per borrower in our portfolio. The GAO has reported that the average consolidated loan under the Options program is $12,232 with the GSL portion of that averaging $7,179 and the National Direct Student Loan portion averaging $2,488. To the extent the large balance loans are taken from our student loan portfolio, we are marginally less able to continue to acquire and service small balance loans. As I am sure has been stated to this Subcommittee many times before, the cost of servicing a small balance loan is roughly equivalent to the cost of servicing a large balance loan while the income streams are, of course, substantially different. To the extent that we lose the very attractive income streams generated by large loans, it will become necessary for our Corporation to reconsider our policy of purchasing loans at par irrespective of the average individual portfolio balance. To the extent that we are forced to replicate the par purchase requirements of Sallie Mae (i.e., average loan balances in excess of $4,500), we will severely impact the origination of the smaller loans within the Commonwealth. This would be an extremely serious problem in Kentucky because we do have a large number of small loans originated each year within the state. To illustrate this point, the Corporation's portfolio as of March 31, 1983, had an outstanding principal of $179,477,000 and an average outstanding indebtedness per student of $3,003 representing 59,766 student borrowers. Clearly, this portfolio has a number of loans which are small balance loans and, based upon my current understanding of the Sallie Mae par purchase requirements, the entire portfolio would not qualify for a Sallie Mae purchase at par.

The GAO Report indicates that data is not readily available to identify persons who could benefit from loan consolidations. Since the guarantee agency in Kentucky currently has terminals located in several major educational institutions in the

Commonwealth and is rapidly expanding on-line communications with the educational institutions and lenders, we believe we would have the capability to readily identify persons who have holdings under the guaranteed program and the National Direct Student Loan program that would qualify for loan consolidation. Whether this makes it desirable for the agency to have the consolidation authority is, of course, dependent upon whether the consolidation program is modified in ways to more reasonably accommodate the consolidation of NDSL with GSL. To the extent such consolidations are expanded under the current statute, the increased cost of special allowance payments associated with an efficient borrower identification system would be substantial, if not prohibitive. However, one of the related benefits of such capability is that most of the data needed to consolidate loans would already be within the consolidating agent's data processing system, thus providing cost savings to the consolidation program. An additional potential benefit to extending the consolidation program to agencies is the demonstrated capability of state agencies to keep default rates at reasonable levels while providing broad access to the loan program.

J. Recommendations.—Based upon review of the GAO study, and the testimony by Dr. Edward Elmendorf before the Subcommittee, and review of Sallie Mae materials relating to the Options program, I would recommend the following to the Subcommittee:

(A) The current legislation should be amended to provide for utilization of a weighted average interest rate rounded up to the nearest integer. This will reduce the special allowance payment obligation to the Federal Government in all cases except where disproportionately large NDSLs are included within the consolidated loan. Also, the administrative difficulties of dealing with innumerable loan rates involved in computing special allowance payments will be substantially reduced for the Department of Education. Subjectively, this methodology would probably yield rates ranging between seven and 10 percent. The Subcommittee may, also, wish to consider a floor interest rate of 7 percent on all consolidated loans as a way of discouraging consolidation by borrowers who may be predominantly financed by NDSL.

(B) The legislation should incorporate repayment extension periods based upon the applicable aggregate loan balances. The repayment schedules and methodologies developed by Sallie Mae in cooperation with the Department of Education seem to me to be reasonable for incorporation into the Act. An alternative would be to extend to the Secretary the authority to regulate the extension periods.

(C) The legislation should delete the provision of administrative cost allowances on consolidated loans and should, also, delete consolidated loans from the reinsurance trigger. In conjunction with this, the legislation should prohibit the charging of insurance premiums on loan consolidations but should permit loan balances to be considered in determining adequacy of any loan guarantee reserves. I am sure that many of my peers in the guarantee agencies and secondary market agencies will disagree with this recommendation. However, speaking only for Kentucky, we believe that there are no substantial increased insurance costs or servicing costs associated with consolidated loans. For agencies which insure and service loans for holders, the potentially available income stream from such large balance loans will be sufficient to offset the absence of either ACA or insurance premiums, particularly, if such loans are not subject to reduced reinsurance rates.

(D) The legislation should require that all loan consolidation agents (i.e., Sallie Mae, state agencies, etc.) offer consolidation benefits to qualified borrowers who are delinquent up to 60 days on loan repayments. If, in fact, a principal justification for offering loan consolidation is to reduce defaults, then it seems imminently reasonable that borrowers who are experiencing difficulty in repayment ought to be the principal beneficiaries of the program. I would be in favor of extending consolidation benefits at any time prior to the occurrence of a default but recognize, under the current Sallie Mae methodology, that this could lead to very difficult monitoring problems to ascertain that loans which are being consolidated have not previously been the subject of a default claim.

(E) As an alternative to the recommendations in (C) above, the Subcommittee may wish to simply provide that all loan consolidations be insured directly by the Secretary. This would simplify the loan consolidation program and make it more manageable by the Department. My primary concern in this respect is that the Secretary, because of cost containment pressures, would attempt to regulate the program so tightly as to discourage many eligible participants. Additionally, I am concerned that Sallie Mae, as a result of both size and proximity, would exert undue influence over the program. On balance, however, I believe this direct insurance approach is the preferable course for the Subcommittee to follow.

(F) The legislation should limit consolidation rights to lenders which have insured or own at least one note made by the borrower. The effect of this would be to substantially reduce data acquisition costs by ensuring that the loan is consolidated into the existing billing and collection system rather than added to an entirely new servicing system. In the event a qualified student does not have any note owned by an authorized consolidation agent, the student should be permitted to go directly to Sallie Mae for the loan consolidation. A requirement for disclosing whether or not consolidation services are available could be incorporated into the notification necessary when any loan is made or purchased by a secondary market.

(G) The legislation should delete all but in-school deferments but permit forbearance for up to one year. This will prevent the Federal Government from having to assume both interest subsidy and special allowance costs for anything other than a return to enrollment. Additionally, the forbearance procedures are very effective in reducing defaults.

(H) The legislation should correct the Section 427 requirement that consolidation loan checks be made payable to students and require instead that such checks be made directly to the holders of the loans to be consolidated. Additionally, the legislation should make the several other technical corrections requested by Dr. Elmendorf in his recent testimony to this Subcommittee. Of particular concern is the notwithstanding clause cited on page five of Dr. Elmendorf's testimony. My concern is that on the basis of this clause Sallie Mae and any new consolidation agents could choose to ignore other provisions of the statutes.

(I) In conclusion, and most importantly, the legislation should leave Sallie Mae, secondary markets, other lenders and guarantee agencies in equal positions to provide consolidation services to borrowers. To leave any of the entities with competitive advantages substantially increases the risk that the other entities will not have the continued capability to service low balance loans and/or to meet servicing costs on their current portfolios.

4. Comments regarding the General Accounting Office Loan Consolidation Study.—In my opinion, the GAO Study accepted and utilized bad assumptions, is inconsistent and fails to address in any depth the two principal areas of inquiry—program costs and impact on defaults. On page 10 of the study they state an inability to come up with precise cost figures for extending loan consolidation authority to the states because of the difficulty in obtaining reliable information on several of the elements needed to compute relative costs. On page four of the study they conclude it is too early to assess the Option program's impact on loan defaults. They completely fail to address the benefits of the reduced special allowance payments which result from tax exempt financing of student loans generally and, also, fail to make the point that consolidation of a loan currently subject to the reduced special allowance may, in fact, cause the Federal Government to incur both the loss of revenue attributable to issuance of the tax exempt securities and the increased special allowance payments attributable to purchase of the loan by a taxable entity. Additionally, all the cost data and most of the assumptions incorporated into the study were provided by Sallie Mae and were not sufficiently justified as to reasonableness. For example, on page three of the study, there is an assumption that investors incur no expenses associated with the purchase of Sallie Mae securities, and, therefore, pay federal income taxes on the full amount of interest earned. While this may or may not be a good assumption, it should be pointed out that Sallie Mae is exempt from state, local and District of Columbia taxes and that there is, therefore, a potentially substantial loss of revenue associated even with Sallie Mae financing. Additionally, also, on page three, there is an assumption that added special allowance payments will exceed savings resulting from fewer defaults. While that would appear to be a reasonable assumption, it is too general to be of any substantial benefit. What will be the magnitude by which special allowance payments would be expected to exceed default savings? I would suggest that a more studied inquiry could answer these and the several other questions raised which have been presented to the committee.

Again, I express to you my appreciation for this opportunity and want to close by strongly recommending that loan consolidation benefits be extended to guarantee agencies, secondary markets and direct state lenders.

STATEMENT OF PAUL P. BORDEN, EXECUTIVE DIRECTOR, KENTUCKY HIGHER EDUCATION ASSISTANCE AUTHORITY, AND EXECUTIVE DIRECTOR, KENTUCKY HIGHER EDUCATION STUDENT LOAN CORP.

Mr. BORDEN. Thank you, Mr. Chairman. I am Paul Borden from Kentucky. Since none of my friends here at the table volunteered, I guess I will go first.

I will simply summarize my remarks and request that the full statement previously provided to you be incorporated into the record.

I find that in many respects my testimony is actually a summary of some of the other things that you have heard here this morning. In Kentucky I am, perhaps, in an unusual position, being the executive director of the guarantee agency and also the director of a secondary market and direct lending entity so I come to you with some perspective from all three of those entities as they participate in the guaranteed student loan program.

We do presently in Kentucky have the necessary administrative capabilities to insure, make, purchase, and, in our opinion, consolidate loans. We have been a leader under the federally insured program for a number of years prior to in 1978 converting to a guarantee agency State. So we do have some experience directly applicable to the private lender participation.

We have developed over that period of time an extensive data processing capability. We do capture extensive data on all of the people participating in any aspect of the loan programs. So we think we have within the system virtually all of the data that would be needed to effect consolidations.

Additionally, we do have terminals out with many lenders in the State and also at educational institutions in the State so that the problem of identification of borrowers eligible for consolidation could, we think, be dealt with effectively in Kentucky.

The invitation from the chairman gives the opportunity to address three specific issues. One is the desirability of extending consolidation benefits to the agencies. We believe that it is not only desirable, but that it is necessary that consolidation benefits be extended.

There have been statements made this morning to the point that there are no or inconsequential increases in cost as a result of the loan consolidation program. I will call your attention to the table on page 4 of my testimony which does show that consolidations by Sallie Mae of student loans which are presently held by tax-exempt entities does result in substantial increased cost in terms of special allowance payments on those particular loans.

I guess that could be rationalized that the tax-exempt securities would then be retired. But I would suggest that that loss of revenue cost is effectively a cost that has already occurred and that the causes of the structure of the tax exempt financing, it is very unlikely that those securities would be, in fact, retired following consolidation.

The current monopoly with respect to consolidation also increases a special redemption risk perception by borrowers. That risk being that if the options program is highly successful, and as a

result, many loans are prepaid, as in the housing industry, that it would be necessary to call bonds.

So, while I don't think that is a very good assessment of the tax-exempt financing because we don't have the interest rate risk that the housing industry has, it is certainly a real perception on the part of investors.

Perhaps a more important area which makes it desirable for us to have the capability to consolidate loans is the effect that the current loan program has on the average loan balances. We have to keep the high balance loans in our portfolio in order to be able to purchase and continue the availability of the low balance loans. The income streams are very, very different and with respect to the Student Loan Corporation, the secondary market in Kentucky, to the extent that we see the large balance loans being taken from us, we will have to reconsider the policy of purchasing all paper at par because those very small loans simply would not support the servicing costs related to them.

Finally, I think, if you examine the statistics, you will find that the State agencies, be they guarantee agencies secondary markets or direct lenders, do have a very good record in the administration of the student loan program and do have the capability to keep the default rates low.

Our recommendations I will go through very quickly. They are outlined specifically in my statement. I believe we ought to use a weighted average interest rate because that considers both the NDSL loan and it also considers the higher interest rate HEAL loans. There is some of all of those consolidated loans. I think there is benefit to tying loan consolidation to an entity which is already the holder of one of the loans because it does have the benefit of reducing cost.

I think there ought to be careful consideration of limiting deferments to inschool periods and I think that on consolidated loans there ought to be some procedure for giving at least some limited forbearance in periods of financial difficulty. I do think that we need to have the statutory difficulty to make consolidation checks payable to the holders.

Finally, and most important, I think that you need to leave all of the participants in an equal position with respect to loan consolidation. To the extent that we have a capability to offer consolidation services similar to that, to Sallie Mae, to Citicorp, or to any other entity, I think you are providing the very best service to the students of the country because access will increase to this particular benefit.

Mr. Chairman, I appreciate this opportunity and will be happy to answer any questions at the conclusion.

Thank you.

Mr. GUNDERSON. Thank you.

Mr. Madigan.

STATEMENT OF JOHN E. MADIGAN, EXECUTIVE DIRECTOR, RHODE ISLAND HIGHER EDUCATION ASSISTANCE AUTHORITY AND RHODE ISLAND STUDENT LOAN AUTHORITY

Mr. MADIGAN. Thank you. My name is John Madigan. I am executive director of Rhode Island Higher Education Assistance Authority, a guarantee agency, and also executive director of Rhode Island's Student Loan Authority, a secondary market.

I am very grateful to have this opportunity to address the matter of student loan consolidation and the possibility of having the opportunity for such consolidation extended to State agencies, particularly those agencies involved in the business of providing student loan secondary markets for their local lenders.

I have had the opportunity to read the statement provided the subcommittee by Mr. Morton Henig of the General Accounting Office and, in fact, have had the opportunity to express my own views to members of Mr. Henig's staff on the telephone during the development of that report. I do concur with many of his findings.

First of all, let me say that I believe loan consolidation is important in both easing the burden on students who may have incurred substantial debt and in avoiding defaults in those cases where students have not reached the earnings potential they hoped for when they accrued such debt.

I would certainly not want to see the consolidation privilege eliminated by failing to extend authorization for the program beyond August 1983.

While I particularly wish to address the need to expand eligibility to the States rather than have only Sallie Mae authorized to operate this important function, I do feel a bit like the person who appeared before Solomon in his dispute over the rightful parentage of the child. I do believe it would be better to lose the right of parentage than to have the child die.

Happily, consolidation, unlike children, can be divided amongst the contenders and the splitting can provide renewed health and vigor to the program.

Rhode Island has been operating a secondary market since late 1981. We have contracted with our local lenders for the purchase of some $100 million of student loans. We must assume that our lenders have committed these loans to us because they see advantage in working in a local market that they do not see in the Sallie Mae market—the advantages of local investment, strengthening the local economy, more flexibility in the size and timing of purchases, and other tangibles or intangibles that appear beneficial to them.

I know you are aware that for many of these loan purchases we do not receive the full special allowance. Loans made October 1, 1980, or after and purchased with tax-exempt bond revenues are limited to only one-half the special allowance or a minimum of 2.5 percent on 7 percent loans or 0.5 percent on 9 percent loans.

Because our existing bonds have a 9¼-percent interest rate and because the maximum return that we have been receiving in recent quarters is only 9½ percent, you can see that we are operating on a very slim margin. As a matter of fact, when we consider our servicing costs, we actually lose money on those post-October 1, 1980 loans.

This has the effect of reducing the margin in our overall portfolio and on those loans for which we receive the full special allowance.

Permitting only Sallie Mae to provide loan consolidation exacerbates this problem for us. As you might suppose, lenders tend to hold on to loans during the in-school period when the servicing cost is smallest and to sell loans just before they go into repayment when servicing costs increase to their maximum. It has already happened that upon our agency, purchasing loans about to go into repayment, and incurring the costs of initiating repayment terms, and setting up the repayment activity, we find that Sallie Mae pays off the loan to a consolidation agreement. The startup costs, which we have borne and which might have been amortized over the life of the loan, have instead been incurred without the possibility of being met through future income.

This would not happen if we also could offer a consolidation opportunity to our borrowers.

The second reason for concern is the clear intention of providing debt consolidation only for the higher cost loan plus the expectation that those borrowers most likely to use that opportunity would be those with the higher obligations and therefore the greatest difficulty in paying the higher monthly costs.

If Sallie Mae or any other secondary market purchases principally our higher average loan obligations, we will be left with a lower average loan portfolio. Since loan servicing costs are roughly the same irrespective of the dollar size of the debt, our smaller average portfolio which clearly cause our unit costs to be higher and further limit our ability to operate in a sound financial manner.

We have felt that the extension of loan consolidation to the State agencies—some have felt, rather, that the extension of this privilege to State agencies would somehow increase costs to the Federal Government. Some of this expectation is based at least partially on a mistaken assumption that the Federal Government would be paying administrative costs twice for the same loan.

This would not be true in our case at least since it is not our guarantee agency but our secondary market that would be doing the consolidating and that agency receives no administrative cost allowance other than the income derived in the same fashion as any other holder of loans, banks or Sallie Mae included.

Also, insurance of new loans made to consolidation of old loans should be handled for the States the same as handled for Sallie Mae, through direct insurance by the Secretary.

One point of advantage that might be considered in determining the desirability of extending the consolidation service to State agencies is the fact that secondary market programs are already in touch with the borrower directly at the time repayment begins. To the extent that consolidation is needed and is important, all borrowers for whom the option might prove advantageous should be equally informed about its availability.

Because of our immediate and direct contact with the debtor, both at repayment time and at various times throughout the repayment period, one who needs to avail him or herself of the opportunity wouldn't need to depend on advertisements or secondhand information. We would include consolidation information for all who

had loans falling within the eligible limits and especially for those evidenced difficulties in handling a debt of a given size.

These then are my concerns—to maintain a consolidation program for the benefit of those who need an easing of the burden and thereby prevent default; second, to allow State agencies which are either direct lenders or secondary markets to share the opportunity to offer consolidation without cost increases to us over which we have no control; and finally, to permit all borrowers to become equally familiar with the opportunity to ease their debt burden through consolidation and to do so at those times in the repayment cycle when it is most advantageous to them.

Thank you for this opportunity and I shall be happy to answer any questions.

Mr. GUNDERSON. Thank you.

You have probably been hearing the bells ringing during your testimony. What that indicates is we have a vote in progress on the floor of the House. What we are going to do is temporarily recess this hearing so that we can go and record our votes and come back as soon as we can.

If the panel will just stay informal at the table, we will reconvene as soon as we get back.

[Brief recess.]

[Prepared statement of John Madigan follows:]

PREPARED STATEMENT OF JOHN E. MADIGAN, EXECUTIVE DIRECTOR, RHODE ISLAND HIGHER EDUCATION ASSISTANCE AUTHORITY AND RHODE ISLAND STUDENT LOAN AUTHORITY

Mr. Chairman and Members of the Subcommittee, I am grateful to have this opportunity to address the matter of student loan consolidation and the possibility of having the opportunity for such loan consolidating extended to state agencies, particularly those agencies engaged in the business of providing student loan secondary markets for their local lenders. I have had the opportunity to read the statement provided to the Subcommittee by Mr. Morton Henig of the General Accounting Office, and in fact, had the opportunity to express some of my views to members of Mr. Henig's staff, by phone, during the development of that report. I concur with many of his findings.

First of all, let me say that I believe loan consolidation is an important activity in both easing the burden on students who may have incurred substantial debt, and in avoiding defaults in those cases where students have not reached the earnings potential they hoped for when they incurred such debt. I would certainly not want to see the consolidation privilege eliminated by failing to extend authorization for the program beyond August of 1983. While I wish to address the need to expand eligibility to the states rather than have only SLMA authorized to operate this important function, I feel like the person who appeared before Solomon in a dispute over the rightful parentage of a child—it would be better to lose the right of parentage than to have the child die. Happily, consolidation, unlike humans, can be divided amongst the contenders and the splitting could provide renewed health and vigor for the program.

Rhode Island has been operating a secondary market since late 1981. We have contracted with our local lenders for the purchase of some 100 million dollars of student loans. We must assume that our lenders have committed these loans to us because they see advantages in working in the local market that they do not see in the SLMA market—advantages of local investment, strengthening the local economy, more flexibility in the size and timing of purchases or other tangibles that appear beneficial to them. I know you are aware that for many of these loan purchases we do not receive the full special allowance. Loans made October 1, 1980, or after, and purchased with tax exempt bond issues are limited to only one-half the special allowance, or a minimum of 2.5 percent on 7 percent loans and .5 percent on 9 percent loans. Because our bonds have 9¼ percent interest rate and because the maximum return we have been receiving in recent quarters is only 9½ percent, you can see we are operating on a very slim margin. As a matter of fact, when we con-

sider our servicing costs, we may actually lose money on those post October 1, 1980 loans, which has the effect of reducing the margin even on those loans for which we receive the full special allowance.

Permitting only SLMA to provide loan consolidation exacerbates this problem for us. As you might suppose, lenders tend to hold onto loans during the in-school period when the servicing cost is smallest, and to sell loans just before they go into repayment, when servicing cost increase to their maximum. It has already happened, that upon purchasing loans about to go into repayment, and incurring the cost of initiating repayment terms and setting up a collection activity, we find that SLMA pays off the loan in a consolidation agreement. The costs which we had borne and which might have been amortized over the life of the loan have instead been incurred without the possibility of being met through future income. This would not happen if we also could offer a consolidation opportunity to our borrowers.

A second reason for concern is the clear intention of providing debt consolidation for the higher cost loans only, plus the expectation that those borrowers most likely to use the opportunity would be those with higher obligations and therefore, the greatest difficulty in paying the higher monthly costs. If SLMA, or any other secondary market purchases, principally, our highest average loan obligations, we will be left with a lower average loan portfolio. Since loan servicing costs are roughly the same irrespective of the dollar size of the debt, our smaller average portfolio would clearly cause our unit cost to be higher and further limit our ability to operate in a sound financial manner. Some have felt that the extension of loan consolidation to state agencies would some how increase costs to the federal government. Some of this expectation is based, at least partially, on a mistaken assumption that the federal government would be paying administrative costs twice for the same loans. This does not appear to be true in our case at least. It is not our guarantee agency, but our secondary market agency that would be doing the consolidating. That agency receives no administrative cost allowance other than the income derived in the same fashion as any other holder of loans, including SLMA. Also, insurance of new loans made to consolidate old loans should be handled by the States the same as handled by SLMA—either direct insurance by the Secretary or where feasible, by insurance through a State guarantee agency. While in the latter case, and under present rules, there would be additional administrative cost allowances by the federal government, such payments would also be made if SLMA used a guarantee agency to provide insurance.

One point of advantage that might be considered in determining the desirability of extending the consolidation privilege to state agencies, is the fact that secondary market programs are already in touch with the borrower directly at the time repayment begins. To the extent that consolidation is needed and is important, all borrowers for whom the option might prove advantageous should be equally informed about its availability. Because of our immediate and direct contact with the debtor, both at repayment time and at various times throughout the repayment period, one who needs to avail himself or herself of the opportunity wouldn't need to depend on ads or second hand information. We would include consolidation information for all who had loans falling within the eligible limits, and certainly for those who evidenced difficulties in handling a debt of a given size.

These then are my concerns:

To maintain a consolidation program for the benefit of those who need an easing of the burden and therefore to prevent defaults.

To allow state agencies which are either direct lenders or secondary markets to share the opportunity to offer consolidation cost increases over which the agency would have no control.

Finally to permit all borrowers to become equally familiar with the opportunity to ease their debt burden through consolidation and to do so at those times in the repayment cycle when it is most advantageous to them. I thank you for this opportunity. I shall be happy to respond to any questions.

Mr. SIMON. Mr. Nicholson, executive director of the Indiana Secondary Market for Educational Loans.

STATEMENT OF ROY A. NICHOLSON, EXECUTIVE DIRECTOR, INDIANA SECONDARY MARKET FOR EDUCATION LOANS, INC.

Mr. NICHOLSON. Mr. Chairman and members of the subcommittee, I am pleased to have the opportunity to testify on the student

loan consolidation issue. I will summarize my testimony and ask that the entire statement be placed in the record.

Mr. SIMON. It will be, as will all the others, if they have not already.

[Prepared statement of Roy Nicholson follows:]

PREPARED STATEMENT OF ROY A. NICHOLSON, EXECUTIVE DIRECTOR, INDIANA SECONDARY MARKET FOR EDUCATION LOANS, INC.

Mr. Chairman and members of the Subcommittee, my name is Roy Nicholson. I am the Executive Director of the Indiana Secondary Market for Education Loans, Inc. (Indiana Secondary Market). I am pleased to have the opportunity to testify on the student loan consolidation issue.

BACKGROUND

The Indiana Secondary Market is a not-for-profit corporation which was authorized by the Indiana General Assembly in 1980 and in the same year was designated by the Governor of Indiana to serve as the state secondary market for education loans.

The creation of the Indiana Secondary Market resulted from findings and recommendations of a Task Force appointed in 1979 by the Governor of Indiana. The Task Force was comprised of prominent representatives of the state government, industry, and the education and financial communities of Indiana. The Task Force was charged with determining whether the then current delivery mechanism for education loans was sufficient to meet the demands of the 1980's and beyond. The Task Force accurately forecasted the rapidly escalating demand for education loans, and further determined that the supply of loans would not be sufficient to meet that demand. The Task Force recommended the creation of a state secondary market which would provide liquidity and thereby encourage and enable lenders to satisfy the growing demand for loans.

The Indiana Secondary Market has met the challenge. We have been fully operational since August 1981. We have purchased 43,730 loans totaling greater than $85 million. We have entered into loan purchase commitments totaling $130 million with approximately one-third of the active originators of student loans in Indiana. Those lenders account for approximately 70 percent of the annual student loan volume in Indiana. We have also introduced an ALAS/PLUS Purchase Program and a Lender of Last Resort Program. To the best of my knowledge, all qualified applicants are able to obtain student loans in Indiana. Indiana lenders have increased their annual volume of guaranteed student loans from $30 million in 1979 to a current rate of approximately $122 million per year.

We have successfully financed our loan purchase program by issuing tax-exempt debt during the period of time in which the tax-exempt debt market was at its all time worst. During the same period of time unemployment rates have been at the highest level in forty years and yet we have been able to maintain a default rate below 2 percent of loans in repayment.

We offer a service which students, families, schools, and lenders of Indiana need and desire. Given our success in becoming operational and growing under recent difficult conditions, we are optimistic that we will be able to continue to provide vital support in the future.

EXTENDING CONSOLIDATION

The Indiana Secondary Market strongly supports the consolidation of student loans.

The key elements of loan consolidation are (1) the ability of the consolidating party to act on behalf of a student borrower to aggregate his/her student loan indebtedness under one promissory note, and (2) more importantly, the ability to provide such borrowers with a repayment arrangement at more favorable terms, particularly a longer repayment schedule and therefore lower monthly payments.

The loan consolidation program represents a logical change in the evolution of the Guaranteed Student Loan Program [GSLP] since 1965. Annual and cumulative loan limits as well as the cost of borrowing as evidenced by the interest rate payable by the borrower and the imposition of an origination fee have increased dramatically, however, the maximum repayment term of ten years has not changed.

Eight years ago, a borrower who had accumulated the maximum amount of guaranteed student loan debt ($10,000) would be required to make monthly payments of

$116.11 for ten years. Today, the borrower who incurs the maximum GSL debt ($25,000) would have to make monthly payments of $316.69 for ten years, almost three times as much. Obviously, the addition of ALAS/PLUS debt would significantly increase the monthly repayment obligation. Under the loan consolidation program, the monthly payment on a 20 year schedule would be a more manageable $193.82 and even lower on a graduated payment basis.

There has been a trend in the last few years in the face of governmental budget constraints on one hand and rapidly escalating costs of education on the other hand to impose an increasingly large share of the burden on the student in the form of loans. Inasmuch as the goal is to collect the loans, it makes no sense to blindly enforce unreasonable, inflexible and outdated repayment terms which are more apt to precipitate a default or bankruptcy.

AUTHORIZING STATE SECONDARY MARKETS AND DIRECT LENDERS TO CONSOLIDATE LOANS

The present network of direct lenders and secondary markets, including both state secondary markets and the Student Loan Marketing Association [Sallie Mae], represents a system of support for students, families, schools and lenders which has been eminently successful in ensuring an adequate flow of capital into higher education during a period of rapid increase in demands on the GSLP.

Few would deny that private lenders could not have satisfied the tremendous demand for student loans without the active support of the network of secondary markets and direct lenders.

As the holder of student loan accounts of approximately 24,000 borrowers, the Indiana Secondary Market is frequently requested to consolidate loans on behalf of student borrowers. We routinely contact the other holder or holders of the borrower's loans, however, we are able to aggregate the borrower's loans only in those instances where the other lender is willing to deliver the promissory note for sale and in the event that the other loans are guaranteed by the Indiana guaranty agency. With loan consolidation authority we could take initiative on behalf of the borrower to pay off any loan made under the Higher Education Act of 1965 and execute a new note with the borrower. We could also of course lengthen the repayment period for larger debts.

We have the interest and ability to implement a loan consolidation program on behalf of borrowers served by us. The authorization to consolidate loans however is not simply a matter of being able to provide a valuable service to borrowers to help them avoid a default or bankruptcy situation. In fact, the viability of many secondary markets and direct lenders is threatened by the continued operation of the loan consolidation program in its present form.

To date, the Indiana Secondary Market has been able to purchase all student loans at par, thereby creating no disincentives to lenders who make small balance loans. The average outstanding principal balance of loans in our portfolio is $3,200. Given that servicing costs are approximately equal on small and large balance accounts and that revenues vary directly with account balance, we lose money on each small balance account. The problem is aggravated by the fact that account balances decrease during repayment while operating costs, including wages, rents, costs of supplies and correspondence, are increasing. It is imperative that we have a sufficient number of larger balance accounts which generate surpluses to offset the losses on the smaller accounts.

Under the current loan consolidation program, Sallie Mae has removed from our portfolio $425,000 in loans with an average indebtedness of $6,250, approximately twice the size of our average loan account. Given the relatively high cost of borrowing in the tax-exempt market at this time and the fact that we receive only one-half the special allowance for most loans in our portfolio, the present loan consolidation program operated by Sallie Mae poses a threat to our continued viability. Our ability to repay our outstanding bonds and to secure additional capital could be jeopardized if a large portion of high indebtedness accounts were taken from our portfolio.

At the very least, if we are unable to offer a comparable consolidation program we will be forced to establish certain minimums with respect to loan sizes eligible for sale. This will have the unfortunate effect of discouraging lenders from making smaller loans and may cause serious hardships for vocational and commuter students in Indiana.

On the other hand, we are in a position to implement loan consolidation as an additional service to complement our present services to borrowers and lenders. Our success in encouraging lender participation in the GSLP is evidenced by the fact that in less than two years we have developed working relationships with 157 Indiana lenders which account for approximately $85 million of GSLoans per year. Our

ability to operate a responsible secondary market is further evidenced by a default rate of less than 2 percent.

LEGISLATIVE CHANGES

I recommend that the authority to consolidate loans be extended beyond August 1, 1983 and that state-designated not-for-profit secondary markets and direct lenders, as well as Sallie Mae, be authorized to participate in a loan consolidation program. The existing network of secondary markets and direct lenders has served all parties extemely well. The continued strength and viability of the current system requires a shared responsibility for loan consolidation. Sallie Mae and the state-designated entities together can best effect the maximum benefits of the loan consolidation program. Loan consolidation reduces the incidence of default and bankruptcy, and represents a logical change in the evolution of the GSLP.

I recommend that the interest rate for consolidated loans not be set at 7 percent which is presently the case, but rather be determined for each consolidation by averaging on a dollar weighted basis the interest rates on the loans being consolidated and rounding the resulting average to the next highest whole per cent. For example, a borrower with $10,000 of 7 percent GSLoans and $6,000 of 12 percent ALAS loans would have a weighted average rate of 8.875 percent and would receive a consolidated loan at 9 percent. The borrower who avails himself of lower monthly payments should not also enjoy the benefit of a windfall reduction in the interest rate as may occur under the present loan consolidation program.

I recommend that the minimums for determining eligibility for consolidation be eliminated, so long as the length of repayment periods is determined by aggregate loan amounts. For example, under the current program if a borrower owes two lenders $2,000 each, his or her loans are not eligible for consolidation because of the $5,000 floor. The Indiana Secondary Market would like to be able to act on behalf of the borrower in that case to consolidate his loans into one $4,000 account. The borrower would nevertheless be required to repay the debt within the current ten year maximum period.

Finally, I recommend that consideration be given to reducing the level of special allowance payments made by the Federal government with respect to consolidated loans. I believe that loan consolidation, including extended repayment periods, is a necessary change to assist in controlling default and bankruptcy claims, and represents fair and reasonable treatment of individual borrowers who have been required to carry an increasing share of the rising costs of education. I understand that extending repayment periods increases the government's liability for special allowance payments. Recognizing the conflict between the need to offer extended repayments on one hand and the increased cost to the Federal government on the other, as well as the "profitability" of consolidated loans, I would support a reduction of the level of special allowance payments on consolidated loans.

Thank you.

Mr. NICHOLSON. Thank you.

The Indiana Secondary Market has successfully financed its loan purchase programs by issuing tax-exempt debt under extremely difficult market conditions. During the same period of time unemployment rates have been at record levels and yet, we have been able to maintain a default rate below 2 percent of loans in repayment. We offer a service which the citizens of Indiana need and desire.

The Indiana Secondary Market strongly supports the consolidation of student loans. The board of directors of the National Council of Higher Education Loan Programs is also on record in favor of extending loans consolidation authority to its members.

The loan consolidation program represents a logical step in the evolution of the guaranteed student loan program. Annual and cumulative loan limits as well as the cost of borrowing, payable by the student borrower have increased dramatically. However, if the maximum repayment period of 10 years had not been changed.

Today the student who borrows the maximum amount has monthly payments almost three times the size as the student who borrowed the maximum 8 years ago. There has been a trend in

recent years in the face of government budget constraints on one hand, and rapidly escalating costs of education on the other hand, to impose an increasingly large share of the burden on the student in the form of loans.

Inasmuch as the goal is to collect the loans, it makes no sense to enforce unreasonable and inflexible repayment terms which are more apt to precipitate a default or a bankruptcy.

From the perspective of the Indiana Secondary Market, the authority to consolidate loans is not simply a matter of being able to provide a valuable service to borrowers to help them avoid a default or a bankruptcy. In fact, the future viability of many secondary markets and direct lenders may be threatened by the continued operation of the loan consolidation program in its present form.

To date, the Indiana Secondary Market has been able to purchase all student loans at par thereby creating no disincentives to small lenders who wish to make small balance loans. The average outstanding principle balance of loans in our portfolio is $3,200. Given that servicing costs are approximately equal on small and large balance accounts and that revenues vary directly with account balance we lose money on each small balance account.

It is imperative therefore that we have a sufficient number of larger balance accounts in order to generate surpluses to offset the losses on the smaller accounts.

Under the current loan consolidation program Sallie Mae has removed from our portfolio $425,000 in loans with an average indebtedness of $6,250, almost twice the size of our average loan account. Given the relatively high cost of borrowing in the tax-exempt market at this time and the fact that we receive on one-half the special allowance for most of the loans in our portfolio, the present loan consolidation program could threaten our ability to repay our outstanding bonds and to acquire additional capital.

If we are unable to offer a comparable consolidation program, we will be forced to establish certain dollar minimums with respect to loans eligible for sale. This will save the consolidation program.

Third, I recommend that the minimums for determining eligibility for consolidation be eliminated as long as the length of the repayment period is determined by the aggregate loan amounts.

For example, under the present program if a borrower owes two lenders $2,000 each, his or her loans are not eligible for consolidation because of the $5,000 floor. The Indiana Secondary Market would like to be able to act on behalf of that borrower to consolidate his or her loans into one $4,000 account. The borrower would nevertheless be required to repay that debt within the current 10-year maximum period.

Fourth, I recommend that consideration be given to reducing the level of special allowance payments with respect to consolidated loans. I believe that loan consolidation is necessary to assist in controlling default and bankruptcy claims. I also understand that extending repayment periods increases the government's liability for special allowance payments.

Recognizing the conflict between the need to offer extended repayments on one hand and the increased cost to the Federal Government on the other, as well as the profitability of consolidated

loans, I would support a reduction of the special allowance payments on consolidated loans.

Thank you.

Mr. SIMON. We thank you.

Our final witness on panel is Mr. Douglas R. Seipelt, the director of the Colorado guaranteed student loan program.

[Prepared statement of Douglas Seipelt follows:]

PREPARED STATEMENT OF DOUGLAS R. SEIPELT, DIRECTOR, COLORADO GUARANTEED STUDENT LOAN PROGRAM

Mr. Chairman and Members of the Committee, I am Douglas R. Seipelt, Director of the Colorado Guaranteed Student Loan Program. I thank you for the invitation to speak today on the issue of loan consolidation in the Guaranteed Student Loan Program.

At first glance, the issue of loan consolidation is simple. It should work to allow a holder of loans to assist students who are heavily indebted to one or more lenders to spread out their length of repayment and to consolidate payments when they owe more than one lender. That's where the simple part ends and the complexity of the Guaranteed Student Loan system takes over. Issues of interest rates, terms, guarantors, lenders, secondary markets, and division of state and federal responsibilities complicate the proceedings.

From a guarantor's perspective, the terms of the present Sallie Mae consolidation system are straightforward. The current guarantor of record is replaced with a federal guarantee and my agency cancels the loan and I have no further responsibilities. It is clear, simple, and to date has been acceptable to Colorado residents.

But, on the other hand, as the number of students facing repayment problems grows, other entities such as the secondary market in my state and individual lenders who hold these students loans are asking why they are not allowed the privilege of consolidating at least their own loans. The secondary market also asks why should they not have the same eligibilities as Sallie Mae under the Higher Education Act since they are structured to perform the same function on a statewide basis. My lenders and the state secondary market are concerned with issues of loan management, portfolio costs, customer liaison and cultivation. In addition, Sallie Mae is perceived as having an unfair market advantage in this area.

In the long term, these issues affect lender and holder decisions as to profitability, restrictions on new loans, and overall participation, thus they cannot be ignored.

As Sallie Mae indicated a little over two weeks ago, in related Congressional testimony, they do not wish to maintain a monopoly in the field of loan consolidation. The GAO study related that numerous state secondary markets were both requesting this authority and capable of administering it. These two facts make me believe, that within established national standards, state agencies and statewide secondary markets should be granted loan consolidation authority.

However, this decision on the part of the Congress, would create some questions that would have to be answered.

1. How would my and other agencies be compensated for the additional length of guarantee commitment (student fees)?

2. Existing bond issues set limits on the types of loans that can be purchased and terms of repayment. Would all new or special bond financing be required to offer loan consolidation?

3. Could statewide consolidators move across state or guarantee agency boundaries to purchase loans?

4. Would my or other agencies receive additional federal administrative allowances to manage the "new loan"?

5. If a state did not participate in loan consolidation, who would be eligible to offer this service to students in that state, Sallie Mae, other secondary markets, other state agencies?

6. Would the students in Colorado receive the same consolidation benefits and eligibilities as students who consolidate with Sallie Mae or in other states?

Assuming suitable answers to these questions and others which might surface are forthcoming, Congress should extend loan consolidation to the states to create parity with Sallie Mae.

This suggestion though does not solve the problem of national or statewide lenders who wish to hold their GSL loans. They should not be asked or forced to sell them to Sallie Mae or state consolidators when they wish to maintain their relationship with the students who have high balance debts.

Keeping in mind the original legislative intent, I propose the following idea to help these lenders.

To understand this recommendation, we must note the distinction between "consolidation" and extended repayment terms. I propose that the GSL statutory repayment language be extended to 15 years for certain students. This gives existing holders the option of performing the stated goal of debt management without utilizing the full component package of "loan consolidation", while maintaining their market share. The following could be the parameters for such a change:

1. Current holders (lenders) could offer students a repayment plan with a 15-year amortization if the student's GSL debt exceeded $7,500.

2. The interest rate for the extended period would remain at the stated GSL borrowing rate, or if long term budgetary costs prohibited the Congress from maintaining the 7 percent or 9 percent rate, the rate could be increased to 9 percent or 11 percent for the extended benefits.

3. Existing lenders or secondary markets could purchase all other GSL loans of the student guaranteed by a single guarantor to meet the dollar minimum of $7 500.

4. The OPTIONS package of Sallie Mae for NDSL, FISL, and GSL mixes would still be available but only to eligible loan consolidators.

Extension of the repayment terms does increase special allowance costs to the Federal Government. However, I believe that increase is not as substantial today; special allowance costs are less than default costs; special allowance rates are down, as a result of lower national interest costs; and a minimum balance combined with potentially raising the interest rate should overcome past opposition. This move would keep GSL loans with their existing lenders and potentially lessen the overall demand for students utilizing the loan consolidation program.

To reiterate, I recommend (1) we extend the "loan consolidation" capabilities of the Higher Education Act to guarantors and statewide secondary markets; and, (2) propose legislation that would extend the length of repayment for selected GSL borrowers to allow national and statewide lenders to maintain their portfolios as they deem appropriate.

I thank you for your time and consideration and would welcome your comments or questions.

STATEMENT OF DOUGLAS R. SEIPELT, DIRECTOR, COLORADO GUARANTEED STUDENT LOAN PROGRAM

Mr. SEIPELT. Mr. Chairman and members of the committee, I thank you for the invitation to be before you today. Rather than reading my testimony, I would request that it be entered in the record——

Mr. SIMON. It will be.

Mr. SEIPELT [continuing]. And try to respond to some of the general comments that my colleagues here have made rather than going through my prepared text.

I believe the issue of loan consolidation is out in front of us for some very good reasons. There are some major concerns that I as a guarantor in the State of Colorado have and also the lenders in my program in Colorado and also the direct secondary market in the State of Colorado.

The issues that have been brought in front of you this morning concerning the repayment problems of students, the problems of bond indentures as they relate to potential payoffs, as Mr. Borden has indicated, the problem of lenders not being able to consolidate debt with students that they have are all important issues in the program that loan consolidation brings to bear as it relates to the issue of whether Sallie Mae is the only loan consolidator in the country and should that extension be granted to States' guarantor agencies and secondary markets?

I think I would like to draw your attention back to just a little history on loan consolidation which many of you well know. The issue of loan consolidation arose, in my opinion, for two reasons.

No. 1, the issue of students who were indebting themselves to a number of different programs, the national direct or national defense student loan in the old days, the guaranteed student loan and the federally insured student loan program.

There was an issue amongst many students and Members of Congress that students were getting into so many programs that the issue of their repayment terms and privileges could become an issue for potential defaults or the ability to repay. So the issue of loan consolidation then was created to solve that problem.

As an offshoot to that, and one of the considerations that I would like to put in front of you today, was that at the time we were making that decision, you were also making the decision concerning an issue of the indebtedness level of students under the guaranteed student loan program. We had, at that point in time, increased the debt limit of a student capable of borrowing on a yearly basis and also the aggregate limits to the extent that today we have students under the GSL only capable of borrowing a maximum of $12,500 as an undergraduate and $25,000 as a graduate student.

So the issue of the students' ability to repay that in a 10-year repayment program under the concept of the current guaranteed student loan program was very vivid in many people's minds at the point in time that we made the decision of loan consolidation as an eligibility for debt repayment.

I think that the dilemma that I have had trying to address the policy question of whether the States are granted, quote, unquote, "the privilege of loan consolidation" versus the issue of extended repayment benefits in the guaranteed student loan component of that issue has been difficult for me because I do not have another vehicle in which to really address the issue.

The only way that the problem of the guaranteed student loan component of this issue in terms of the high debt balance of students and also the issue of my secondary market as it relates to debt that they have incurred under the program to purchase guaranteed student loans and the issue of lenders in my State as it relates to their ability to maintain rapport and customer relationship with students who they have lent their funds to, who they wish to continue having a rapport with those students through the repayment process comes to bear.

That is why my testimony has related that as long as the only vehicle for this discussion in terms of trying to solve the concerns of the Colorado lenders in the secondary market relates to the issue of extending repayment benefits under the guaranteed student loan program so that students have the ability to consolidate that debt, I believe the issue then should be that the State of Colorado and other lenders under our program and State agencies do need to have the benefits of loan consolidation.

But I would also draw your attention back to the discussion that we had in those days about extended repayment benefits in the guaranteed student loan program. One of the issues that we addressed—we did not, as you will remember, feel that it was important at that point in time to extend the repayment benefits because of the Federal costs in the outyears as it relates to the costs of the special allowance.

At that point in time we were looking at special allowance rates which were almost equal to the cost of the direct subsidy. Special allowance at that time was 7½, 8, 8½ percent, 9 percent, as it related to the 7 or 9 percent consideration of the direct subsidy.

Therefore, the outyear costs and the budgetary costs for extending repayment terms in the guaranteed student loan program were quite significant. I believe at this point in time that I am not sure that that budgetary constraint is still there, as it relates to the issue of extended repayment benefits in the guaranteed student loan program.

Therefore, my recommendation is that I believe that we must have a vehicle to address the concerns of the secondary market in my State and the lenders in my State. I do not believe that those two entities should be precluded from continuing a relationship with students who they have lent to under their college degree as it relates to their repayment privileges and not be forced or otherwise to sell that loan off to a loan consolidator whether it be the State agency, whether it be Sallie Mae or some other entity that is given that power.

I think it's important that we also, at the same time, address the policy question of extending consolidation benefits to the States, that we address the concern of extended repayment benefits in the privileges of the guaranteed student loan program as one component of the issue of loan consolidation as it relates to NDSL, federally insured loans, potentially ALAS loans and also the guaranteed student loan component.

In my paper I have given you some recommendations as it relates to that and I would like just for a second to go through those.

I believe that the issue for my lenders, at least the direct lenders in my State, the commercial lenders, that issue would be solved if we were to grant them the condition of extended repayment benefits under some constrained lending requirements such as the extended repayment benefits would be for a 15-year period under the guaranteed student loan program and that we commit those repayments to only students who have a consolidated GSL debt of at least a $7,500 loan amount.

I believe also that to address the concern, I personally believe that the interest rate as it relates to the consideration of special allowance today could remain the same for this extended repayment benefit, but if it was the consensus of the Congress that for budgetary constraint that that cost was too great to offer these extended repayment benefits, then I would propose that we do then raise the interest rate for the consolidated repayment loan under GSL to a figure of 9 percent for 7 percent loans or a figure of 11 percent for 9 percent loans and there is nothing magic about those two numbers.

I think those two numbers would be set as it relates to the budgetary constraints or the cost to the Federal Government under the special allowance program.

I think that at that same time if you were then to grant the consolidation benefit to the State of Colorado or the secondary market in the State of Colorado that the needs of Colorado residents as it relates to consolidating NDSL's, FISL's and GSL's could well be met, but the other factors of lenders in my State who wish to main-

tain their relationship and customer rapport with their lenders would also be solved at the same time.

I think also, at least in the State of Colorado, what you would find is that the need of loan consolidation as an entity would be lessened because the major component in my State of indebtedness is in the GSL faction of this equation not in cross referencing a number of two or three or four different other programs.

With that, Mr. Chairman, I would be more than happy to answer any questions you might have.

Mr. SIMON. Thank you very much.

Let me just make a few comments as I sense where we are.

No. 1, as an accommodation and a convenience for those who have borrowed, this is a desirable thing, but probably not a high priority thing from the viewpoint of the Federal Government.

No. 2, on the cost factor, I have a hard time getting hold of anything. Is this going to cost the Federal Government $2 million, $80 million? I don't know. That is a concern.

No. 3 goes beyond the accommodation factor. To what extent, when we have consolidation do we help institutions to make money available to other students through NDSL repayment? To what extent are we encouraging the lenders, the banks, to stay in the field?

I don't know whether the gentleman from Citibank who testified is still here.

Mr. BIKLEN. I am.

Mr. SIMON. If you don't mind pulling up a chair and if I can call on you again—I wonder if you would comment on those general kind of categories and specifically, I would be interested in what you think the perspective is, not only of Citibank, but for banking institutions' attitude toward this whole question. Maybe if I can refer this to you first.

Mr. BIKLEN. Yes. I think I can speak for most of the other lenders. As I indicated earlier, I have spoken to a number of other lenders on this subject and I think there is a real concern, given that lenders cannot offer this particular product or service, that they are put in a position of really competing unfairly. What we find happening is that we are losing our high balance loans. The fact remains that those loans cost us the same to service as any other loan does. That is a real concern to us.

I think complementing that is the fact that we lenders have had experience in consolidating loans, given that any time you make more than one loan to an individual you have to consolidate those loans into one when they go into repayment and you negotiate a new repayment schedule and so forth.

So this is not entirely new although this would be a somewhat different process. The other point I made—earlier was that I think in an administrative sense that having the lenders participate in this program I think would ease the burden on students. There would be no need necessarily to bring in an additional party that would have to purchase the loans. One of the lenders that already have them would simply buy the rest of them. So you wouldn't have to bring in another party and it would just be a lot simpler to effect.

Mr. SIMON. All right.

Any comments from any of the others on my reactions here?

Mr. MADIGAN. If I might, Chairman Simon.

Mr. SIMON. Yes.

Mr. MADIGAN. I understand what you mean when you say this is a matter of accommodation and probably not a matter of high priority to the Federal Government, but if I might have you consider some of the extreme cases. We happen to be in Rhode Island, a direct lender in the HEAL program, and we have a number of students who are going into a variety of health professions institutions.

One of our greatest concerns recently has been students to whom we have been advancing as much as $10,500 a year to attend veterinary school. They are graduating with a $20,000-plus debt, not to mention other debts they may have incurred either in GSL or NDSL in undergraduate school or even in their veterinary program for costs other than direct tuition. We have students graduating with $60,000 worth of debt and the typical starting salary for a new veterinary is about $18,000.

It seems to me that we have to express concern for the ability of those students to meet that kind of obligation and consider it something more than an accommodation. It becomes a necessity, I think, to avoid the excessive costs that might be incurred in bankruptcy and other kinds of default. Many of these students, their first contact is to say, "I have a big problem and I have to have graduated repayment," and we are attempting to deal with that.

But I think the fact that we offer the program and that students take advantage of it in anticipation of some great capacity to repay and then to find out that this hasn't occurred and that they need help becomes something that has to be of considerable social concern.

Mr. SEIPELT. Mr. Chairman, I would like to follow up on Mr. Biklen's comment. My testimony and my proposal is directly related to the structure of the State of Colorado as it relates to the lending community. I have concerns for the secondary market in the State of Colorado because they are a purchaser of student loans as it relates to liquidity in the State of Colorado.

On the other hand, my secondary market in Colorado is not a direct lender. All of the loans made in Colorado, almost $300 million to date in the last 3 years, are direct loans made by lenders in the State of Colorado, about 225 individual lenders. Over 80 percent of that paper is still held in those lenders' portfolios. Most of those lenders that do not sell to the secondary market in Colorado have participated in the program because it is a customer relationship program. It is a program that they utilize to both cross-sell other lender services in relationship to other loans, deposits, demand deposits and other things, that they have visualized the guaranteed student loan program as part of a generalized credit package to an individual and a family.

Therefore, it is very important to them if their consideration, both from a cost factor and a participation factor, is whether or not they can maintain that graduate student's indebtedness after the student has gotten out of school and goes into repayment. If they cannot maintain that account for the next 10 or 12 years in the repayment status and potentially make other loans and other credit

and other banking relationships available to that customer then they, I feel, are not totally willing to participate on the front end in making that loan in the first place.

So I have some considerable concern about their eligibility to participate in this, quote, unquote, "loan consolidation mechanism."

Mr. NICHOLSON. Mr. Chairman, I would like to comment on your first two points as well and tie them together. The matter of loan consolidation or extension of repayment as a convenience, I want to concur with my colleagues that it really is more than a matter of convenience. In the long run, the Federal Government is apt to save money, not lose money by avoiding the defaults that come with forcing repayments into a 10-year period.

From day one of the program, 1965——

Mr. SIMON. If I may interrupt. One of my concerns here is that it looks to me like maybe we are helping the students who are not likely to default anyway. Those who have defaulted are not going to get consolidation. Is that correct?

Mr. NICHOLSON. Yes.

Mr. SIMON. Those who have defaulted are not. So what we are doing is that we are taking the low-risk student and providing assistance?

Mr. NICHOLSON. There is an argument, Mr. Chairman, that the high indebtedness students are more apt to repay their loans, that the default rate on those loans is lower. I think that's documented.

On the other hand, there are many students—and we have experienced this situation—who have graduated owing a lot of money and simply cannot repay it within the 10-year period. In 1976, the most you could borrow in this program was $10,000. Now in GSL alone you can borrow $25,000. Now your payments will be three times as high. It will be over $300 a month as soon as you leave school and enter your base period.

So I think there's a need. But there is also very definitely a cost to the Federal Government. On a 10-year repayment on a $20,000 the Federal Government will pay $3,000 in special allowance over a 10-year period on a $20,000 loan. Now if that $20,000 worth of loans is consolidated for 20 years and extended for 20 years, the special allowance payments would be five times as much; it would be over $15,000. So there is a very real cost to the Federal Government of this program.

I would like to suggest that that cost is greater than it needs to be. I think that there is a need for loan consolidation and recognizing that need, I think that there ought to be a concession made on the part of those people who think there is a need, recognizing the budget problems of the Federal Government, that the special allowance on consolidated accounts be reduced.

The Indiana Secondary Market is able to operate in the black buying accounts that average $3,200. Sallie Mae is able to generate handsome profits buying accounts that average $5,000. The accounts that we are talking about here are averaging well over $10,000. There is a profit potential there that can be reduced without creating significant disincentives for those of us who wish to consolidate loans on behalf of students.

Mr. SIMON. Yes?

Mr. BORDEN. Mr. Chairman, I, too, would like to make some comments. I don't think that anyone else has addressed the relationship of the educational institutions and the possibility through loan consolidations of, in effect, prepaying NDSL's and putting more money into circulation in the institutions.

I did, in fact, talk with a person at one of our major institutions in Kentucky yesterday on this particular point. To his credit, I guess, he called me rather than me calling him. The point he was making is that he can not cover his servicing costs on NDSL at the 3-, 4-, and 5-percent incomes and he, therefore, is very interested in running some social security number sorts with us for us to tell him which of those borrowers have GSL's so that he can then send lists of names to Sallie Mae.

I explained to him that we rather like those high balance GSL's because they make it possible for us to make those low-balance loans available to his students.

We could do this. We could identify a lot of people who are eligible for consolidation and probably need consolidation but it's economically not a very good decision for us to cream our own portfolios of the high-balance loans.

So there is a great interest on the campus in that area of consolidation.

On a couple of other points that you mentioned, the cost factor, I agree that it is very difficult to get a hold on that, but would again refer to the table on page 4 of my remarks. While it's difficult to get a hold on the cost of setup, the cost of advertisement, acquisition, it's not too difficult to get a hold on the cost by which special allowances increase when a loan is consolidated out of a portfolio that has been financed in the tax-exempt market.

We get half the special allowance; the non-tax-exempt people get a full special allowance. So certainly, to the extent that we are losing accounts, the special allowance is going up substantially currently.

I think if the justification for the program is to have an impact on defaults, we ought to simply require the people who are 60, or perhaps even more days delinquent, be eligible for consolidation as well. I recognize there are some difficulties in that, but certainly I think those difficulties can be managed. I am sure that we could manage 60-day delinquent consolidation in Kentucky.

Finally, you addressed the issue of whether this would help keep lenders in. I agree with the gentleman from Citicorp that it would, because they are very, very aware of servicing costs and they know that if large volumes of loans get consolidated out, that their servicing costs may not be met on those lower balance loans.

So I think you hit three very excellent points with respect to this issue and it seems to me that it's solvable by extending it and by making the law much more specific.

Mr. SIMON. One final question.

A couple of you touched on the need in commenting. I wonder if the other three of you—if I can pull you in as a witness again here, Mr. Biklen—to what extent is this really a need or to what extent is this simply an accommodation that maybe we ought to make, but it is not a high-priority item if the costs are going to be a major factor here?

Mr. BIKLEN. To the extent that it is a need, I think it's difficult to comment on that. We have seen our sales of these things picking up dramatically in the last two months, I would say. I would attribute that primarily to the advertising campaign that has been going on.

In the sense of what is the need out there—and I think this really gets back to how does all of this really tie to the default rate. Would these people pay regardless of whether or not they could do this program? I don't know the answer to that. The only thing I could suggest—and I don't know if this information is available, but as I said earlier, if it were possible to determine at what point are these loans being consolidated, at what point in repayment are they being consolidated and get a fix on that—are they 1 year into repayment, are they 2 years or whatever, and then you could compare that to, if it was available again, the history of defaults that have occurred in the normal GSL and NDSL programs up to that point in repayment. Then we could get an assessment of what is really the impact of this program on defaults and, until we know that, I don't think you can really make the judgment of what is the need for this program.

Mr. SIMON. Any further comments?

Mr. SEIPELT. Mr. Chairman, I believe that the need in this context is sort of like a moving freight train. The statistics to date as it relates to the Sallie Mae loan consolidation numbers are really insignificant as it relates to the total portfolio that is setting out there in the guaranteed student loan program, the NDSL and/or potentially in the ALAS/PLUS component.

I believe though that the circumstances that we are seeing that the gentleman from Indiana proposed is that as we continue through the cohorts of the guaranteed student loan program through the next 3 to 5 years of the massive amount of loans that we put under guarantee in this program, as those loans become due and payable in the repayment sequence, the need for a structured extended repayment, extended potential payoff, students will increase dramatically, because, as we—just over the last 2 years from the guarantee agency perspective, we have increased the average debt per student by over $1,500 per student. That is quite significant in less than a 2-year time period. What we are seeing is that due to the cost of education and other related student aid programs, that debt burden of students is rising and they must continue to borrow as their higher education costs continue. So I believe that the issue may not be as grave and needy today, but in the next 2 or 3 or 5 years, it will increase dramatically.

Mr. SIMON. That's a good point.

Mr. MADIGAN. Chairman Simon.

Mr. SIMON. Yes?

Mr. MADIGAN. There is one other area too that has not been brought up in any testimony so far and that is the problem of potential consolidation for parent loans, which, of course, is a relatively new program. But here is a situation where parents make consecutive loans for 4 years in a row up to a maximum of $3,000 and find that these obligations are accumulating each with its own separate repayment period and potentially with different interest

rates, we already have some parents, of course, who borrowed at 14 percent and then made additional loans at 12 percent.

It may be important to consider the need in that particular area for potential consolidation as well.

Mr. BORDEN. Mr. Chairman, with respect to the need for consolidation issue, I tend to agree completely with Doug's statements that the future need may be greater than the current need.

However, it's one of those kinds of issues where you almost need to legislate good judgment on the part of the people offering to consolidate because we see a lot of cases where students may have only $4,000 or $5,000 in loans and they need an extended repayment period because they either haven't completed the educational program or they are simply in an occupation which won't support those kinds of repayments.

But it's a two-edged sword to the extent that you raise that $5,000 threshold, you are, in effect, limiting the consolidation program to the doctors, the lawyers, graduate students, who have probably gone through the programs and completed many of them and have the highest capability to pay.

To the extent you lower that threshold, you are, in effect, encouraging extensive increases in special allowance payments that would be due from the Federal Government. So, I just sympathize with the fact that it is a problem as to how you solve that dilemma. But subjectively, and based upon our experience with about $179 million in student loans in Kentucky, we see a lot of people who have a need to consolidate some extended and reduced repayment terms, but they are not just above $5,000.

Thank you.

Mr. SIMON. We thank you.

I am going to call on Mr. Penny in a moment, but we may want to get back to you. We are going to have to move rapidly on this now and make some decisions soon.

Mr. Penny.

Mr. PENNY. Mr. Chairman, this may have been covered while I was gone, but I am curious about the competition between all the lenders for consolidating loans and whether that is going to result in the circumstance where Sallie Mae is no longer going to participate in the consolidation at all, if we open it up to private lenders and to direct lenders, to States who might be direct lenders.

Mr. NICHOLSON. If I may, I would like to comment on that.

My colleague from Citibank isn't going to like to hear me say this, but I don't think that it would be a good idea to extend consolidation to all lenders. Lenders would be then highly motivated to take in as many large balance accounts as they can, because, as I said, large balance accounts are profitable accounts.

That will leave those of us who don't have a choice but to buy student loans in jeopardy. We will be left with the smaller balance accounts. We are not in a position of the banks, where if we can't operate in the black or break even at what we do, then we can't go out and make car loans or second mortgages. We are in this one business because basically the Congress has put us there.

We offer a valuable service to citizens of the States. To allow banks, as well as Sallie Mae, as well as State secondary markets all

to compete in this program, I think, would be detrimental to the future of the program as we know it and of its recent success.

Mr. BORDEN. I think one way to perhaps limit that competition is to incorporate a requirement that, the first attempt at consolidation be made by an entity which is a holder of one of the loans to be consolidated. One of the benefits of this is that you substantially reduce the cost of data collection in conversion to the consolidated loan.

Another thing is that if you are dealing with secondary markets or direct lenders, you could require that at the point the loan is made, there be a disclosure as to the capability or the availability of consolidation by that particular lender.

I would then say that if you have a borrower who is eligible that no other consolidation agent holds a loan for that, that person ought to have the capability to go directly to Sallie Mae.

Mr. PENNY. Thank you.

Mr. SEIPELT. Mr. Chairman, could I make one response to that?

I believe, Mr. Penny, that my testimony speaks directly to the issue that Roy just raised. I personally do not believe that it is good public opinion to offer the quote, unquote, "loan consolidation mechanism" to over 1,500 entities in this country as it relates to all the potential lenders—State secondary markets, State agencies themselves.

On the other hand, due to the points that I made before, I think we need to be very careful not to put the lenders, the lenders themselves who put up the money in the first place, many of which hold their loans through repayment, into an untenable situation that they cannot compete with the secondary market in Colorado or the secondary market in Indiana or Kentucky or otherwise, because the issue for them is extended repayment benefits on loans that they wish to hold, not the issue of, quote, unquote, "loan consolidation." So I think we have to be careful not to forget where the funds come from in the first place.

Mr. BIKLEN. Yes. I would echo what Doug just said. In terms of your original question, "What might this do to Sallie Mae?" I still think that there would be a need for Sallie Mae to the extent that they would be making consolidations that might run across guarantor lines, that would run across NDSL—I don't believe they are consolidating HEAL loans now—but I think you would still find that type of need.

Again, in reflecting on what Doug just said, I think what we are really talking about is if the lender has a loan with them, to allow us to make the consolidation, too. I think that's the basic issue. Otherwise, you are at a tremendous competitive disadvantage and you would really have some questions about the program.

Mr. MADIGAN. If I might comment briefly also.

We are really not so interested, at least from my point of view, in competing as we are in protecting ourselves against loss. If we suffer loss, we are in a real difficult situation. As Mr. Nicholson pointed out, we cannot get into other markets. So once those high dollar average loans are gone or once we put loans up in repayment at startup cost and then have those loans bought immediately, we suffer real substantial loss and we have to protect ourselves against that.

Mr. PENNY. I have no further questions.

Mr. SIMON. I think minority counsel has some questions. Mr. Dean?

Mr. DEAN. I would like to ask the panel to comment on a statement made by Mr. Fox earlier.

On page 20 of his testimony he says, "We do not believe that the concept of a weighted average interest rate is a viable one." Mr. Fox goes on to say, "If weighted rates were applied, the number of permutations in combinations of monthly payments would be infinite, and the borrower could not be informed up front of the new payment schedules until after the new promissory notes were generated."

That's the first thing I would like you to comment on. The second one is, "It would be extremely difficult to accurately generate and control the Government interest billing if weighted rates are reported to and must be validated by the Department of Education."

If each of you could comment on both of those, whether you agree or disagree with Mr. Fox, and if you do disagree, why you don't think these are problems with the weighted rate.

Mr. BORDEN. I believe that if you permitted averaging to two or three decimal places, that certainly you would have a great deal of problems. But if you average and then round up to the nearest integer, there should be no problem. In fact, the great majority would be 7-, 8-, or 9-percent loans and we are going to have all of those anyway. There might be some tens if we have HEAL loans involved, and possibly it could go up to 11. But so long as you keep it in that direct relationship of a full-integer interest rate—and the rounding-up would also have the benefit of reducing special allowance costs for the Government—it seems to me that both Sallie Mae and the Department of Education have demonstrated a capability to handle special allowance billings on that basis. It's just adding a couple of other categories.

Mr. NICHOLSON. I can't improve on what my colleague from Kentucky has said. I think he has said it very well.

Mr. DEAN. Please comment on the fact that the borrower will not know the monthly schedule until after the note is issued. Again, it would be a weighted average and the borrowers wouldn't know how much the consolidation amount would be until they got the original notes from the holders.

Mr. BORDEN. I don't really understand that point because when you get the information on the student loans to be consolidated, it's a relatively simple matter to then run that through the machine and see what the total amount to be paid off would be and what the repayments would be on a monthly basis. It may create an intervening step that would add some expense. You get the information in and then you send back to the borrower and say, "If you choose to consolidate, these will be the terms, conditions, and repayment rates for such a consolidation or these are the options that you have with respect to that."

So it seems to me that that should be a problem.

Mr. DEAN. As I understand this—you wouldn't be able to know exactly what the repayment amount would be because you don't know what the balance is if a loan has been in repayment for 6

months. Let's say that one is a 7-percent loan and then you have a couple of 12 percent loans at various other stages. You wouldn't be able to tell the student, depending on how you were going to determine the weighted average, either the interest rate that they were going to be paying or the monthly payment on it. This is because you wouldn't know what the balance was until after you had already sent notice to the holders of those notes and those notes had come in.

Mr. BORDEN. I think that's the equivalent of closure on a bond issue where you are refinancing other debt. You have to pick a point in time at which the consolidation would occur and you reach that agreement or you state that date to the borrower and to the other holders of obligations for the borrower and then you settle up with the prior holders as a part of the closure mechanism.

It's something that many of us have been through and I continue to think that it's not an insurmountable difficulty.

Mr. NICHOLSON. What Mr. Fox has said is correct with respect to the idea that you would average out to two or three decimal places. The picture is changed entirely when you talk in terms of rounding up to the nearest whole percent. With respect to the difficulty for the Federal Government to audit bills, again, he's entirely correct in saying that that would be nearly impossible for them to do, if we were talking about rounding out to one or two or three decimal places. It's not true if we are talking about rounding up to the whole integer.

Mr. DEAN. You would probably double or even triple the number of different interest rates that would be in a portfolio for billing a special allowance.

Mr. NICHOLSON. Yes; that's possible.

Mr. BIKLEN. I think that what he might be getting at there is the fact that if you have one rate or two rates and you know what those rates are going in, an individual would know what their outstanding was and it would be very simple to calculate—based upon the repayment term—what the monthly payments were to be.

On the other hand, if you were going to come up with—if you were going to start averaging rates, you would not be able to refer to a simple table. You would have to go through this weighted average calculation. I think that is what he was getting at there.

Mr. MADIGAN. I might just make the point also that our secondary market already purchases loans in repayment and we do have the capacity for determining what the balance would be.

Mr. DEAN. Let me ask one last question.

Do you see problems with interfacing a weighted average interest rate on these loans with the graduated repayment program? I understand that would be extremely complex and be nearly impossible to implement. Do you think that you could implement this?

Mr. NICHOLSON. Yes, Mr. Dean, I do. Once the rate has been established at 8 or 9 or 7 or 10, then the matter of applying the graduated repayment formula is the same whether we are talking about a 7-percent loan in the first place or an 8 or a 9. That's what computers are for. [Laughter.]

Mr. MADIGAN. We work with a servicer and I checked with him specifically to see what kind of problems he would have. Let me say up front that he admitted that it is a very difficult problem to

solve initially, but it is a matter of solving how to program it and once it is programed it no longer becomes a difficult problem.

Mr. BORDEN. Maybe the report language ought to specify that Sallie Mae ought to share that technology with the guarantee agency. [Laughter.]

Mr. SIMON. We thank you very much for your testimony.

We may very well be getting back to you for your reaction to what we will be putting together.

Thank you very much. The hearing stands adjourned.

[Whereupon, at 11:49 a.m., on June 8, 1983, the subcommittee was adjourned.]